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[1] In some cases, original copies needed to be photocopied before being scanned into electronic format. All scanned images were deskewed (to remove the effects of printer- and scanner-introduced tilting) and lightly cleaned (to remove dark spots caused by staple holes, hole punches, and other blemishes caused after initial printing).

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Confidential (FR) Class III FOMC

Part 2

December 11, 1997

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Recent Developments

Prepared for the Federal Open Market Committee
By the staff of the Board of Governors of the Federal Reserve System

Confidential (FR) Class III FOMC

December 11, 1997

RECENT DEVELOPMENTS

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DOMESTIC NONFINANCIAL DEVELOPMENTS

Labor market indicators point to continued strong growth of economic activity in recent months. Households evidently have maintained their upbeat attitudes through the recent storms in world equity markets, and growth in real consumer spending remained healthy through November; household confidence has been evident in the market for homes as well. Trends in capital goods orders have remained quite positive, but growth in real fixed investment this quarter appears unlikely to approach the extraordinary pace of the previous six months. Although labor markets continue to be tight and to exert upward pressure on wages, sizable gains in productivity have thus far kept unit labor costs in check. Price inflation has remained low and stable.

Labor Market Developments

Hiring was very brisk in the first two months of the fourth quarter. Payroll employment rose about 350,000 on average over October and November--well above the average monthly pace of the first three quarters of the year. With labor force particpation relatively flat over the second half of the year, the recent surge in employment has caused the unemployment rate to fall to 4.6 percent, its lowest level in almost twenty-five years.

Aggregate hours of production or nonsupervisory workers shot up 1.1 percent in November, as the average workweek jumped more than a quarter of an hour to a high 34.8 hours. Even assuming some dropback in December, the increase in hours for the fourth quarter as a whole would be close to 4 percent at an annual rate.

Private payroll employment rose 409,000 in November after recording a gain of 257,000 in October. For November, payroll increases were widespread across sectors. The service industry accounted for 180,000 of the gain, with temporary help supply contributing almost a third of that increase. Despite anecdotal reports that retailers were having difficulty hiring, that industry posted its largest employment gain in nearly three years. Employment in the manufacturing sector increased 44,000 in November; over the past twelve months, manufacturing payrolls have expanded nearly 200,000.

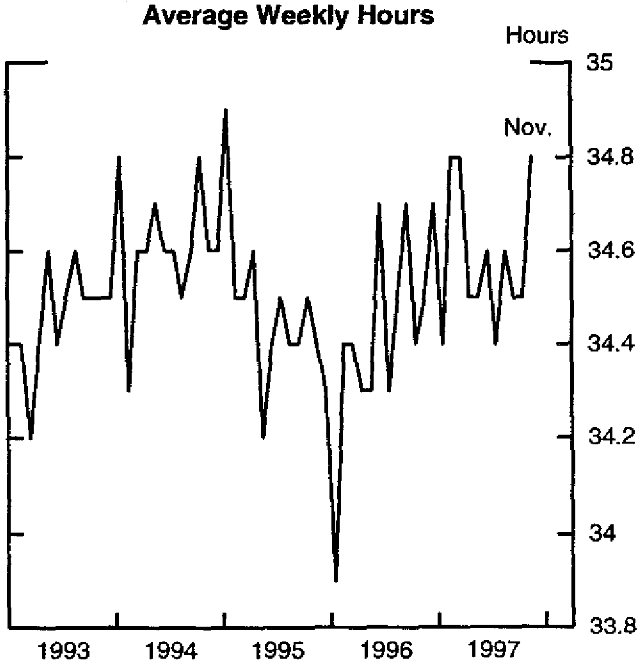
The November household survey painted a similar picture of labor market strength. Employment jumped 671,000 after a period of relatively weak growth. In contrast to anectotal reports that firms

CHANGES IN EMPLOYMENT
(Thousands of employees; based on seasonally adjusted data)

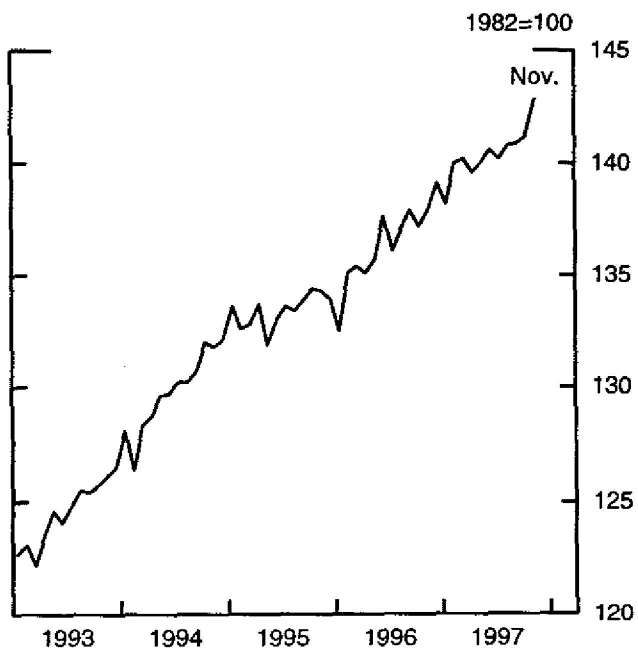
	1995	1996	1997 Q1	1997 Q2	1997 Q3	1997 Sept.	1997 Oct.	1997 Nov.
	---Average monthly changes---							
Nonfarm payroll employment [1]	185	212	228	237	245	300	287	404
Private	176	198	218	206	220	390	257	409
Goods Producing	8	19	43	15	19	6	44	72
Manufacturing	-1	-5	14	10	12	-2	38	44
Construction	10	24	29	4	7	5	8	29
Service Producing	168	178	175	191	201	384	213	337
Transportation and utilities	8	9	39	10	13	184	27	9
Trade	48	60	28	52	63	38	56	129
Finance, insurance, real estate	-1	11	10	14	16	14	24	19
Services	113	98	97	115	109	148	106	180
Help supply services	10	13	17	-17	5	28	4	53
Total government	9	14	10	31	25	-90	30	-5
Private nonfarm production workers [1]	151	168	195	163	161	350	181	342
Manufacturing production workers	-2	-5	9	7	9	3	34	27
Total employment [2]	32	232	440	63	117	-89	179	671
Nonagricultural	51	225	453	61	97	-156	326	593
Memo:								
Aggregate hours of private production workers (percent change)[1,3]	1.7	2.9	4.1	1.7	1.6	0.1	0.2	1.1
Average workweek (hours) [1]	34.5	34.4	34.7	34.5	34.5	34.5	34.5	34.8
Manufacturing (hours)	41.6	41.5	41.9	42.0	41.8	41.9	42.0	42.1

Note. Average change from final month of preceding period to final month of period indicated.
1. Survey of establishments.
2. Survey of households.
3. Annual data are percent change from Q4 to Q4. Quarterly data are percent change from preceding period at an annual rate. Monthly data are percent change from preceding month.

Average Weekly Hours



Aggregate Hours of Production or Nonsupervisory Workers



were hiring an unusually large number of part-time workers for the holiday season, part-time employment, for both noneconomic and economic reasons, actually fell in November. The longer-term decline in part-time employment for economic reasons is consistent with reports that firms are increasingly switching workers from part- to full-time employment.

The labor force participation rate rebounded in November to 67.1 percent--in line with the average over the first three quarters of the year. The fraction of the population not in the labor force but wanting jobs has fluctuated at a low level in recent months, which continues to suggest that the participation rate has little upside potential. Indeed, anecdotal reports indicate severe shortages of workers in some fields--perhaps most notably, information technology. The problem of availability is reported to be particularly troublesome for small business; the proportion of companies reporting to the National Federation of Independent Business that positions are hard to fill has been at a high level in the past several months.

Other indicators reinforce the image of a strong labor market in the fourth quarter. Initial claims for unemployment insurance stayed low into early December. The Manpower, Inc., survey of net hiring strength for the first quarter of next year remained at a high level.[1] Household perceptions of labor market conditions also continue to be very positive, according to the Michigan and Conference Board surveys.

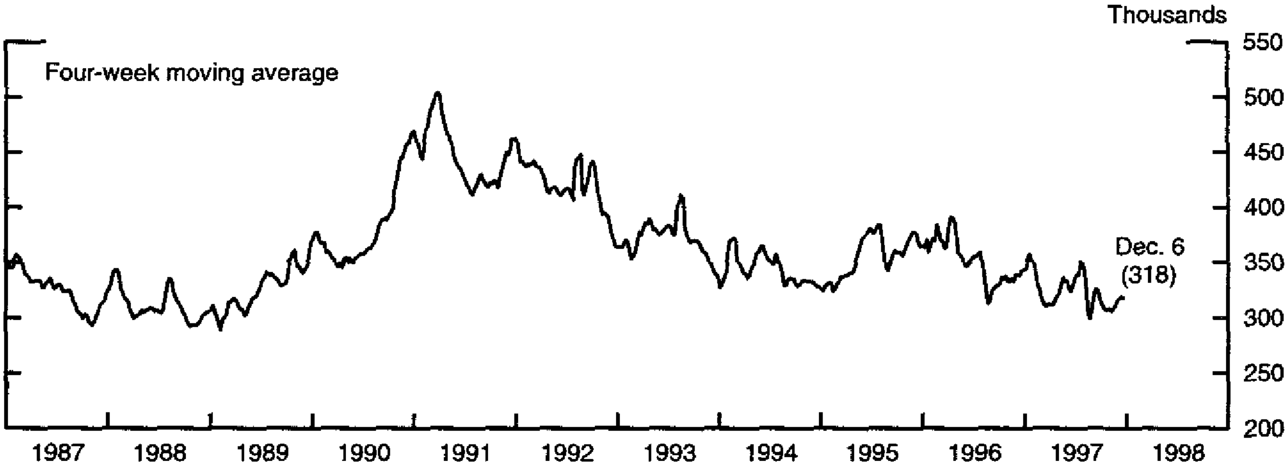
Growth in output per hour in the nonfarm business sector rose 4.1 percent at an annual rate in the third quarter. Over the four quarters ending in 1997:Q3, nonfarm business productivity advanced 2.4 percent, the highest rate recorded in almost five years. Third-quarter gains in labor productivity were particularly large in the manufacturing sector, in which productivity jumped 9.3 percent at an annual rate, and in the nonfinancial corporate sector, in which productivity climbed 6.7 percent at an annual rate.

The sharp rise in nonfarm business productivity in the third quarter was partly due to an especially large drop in the hours of the self-employed and of unpaid family workers. The drop in such hours significantly reduced the measure of all person-hours used by

1. The Manpower survey tends to be a better indicator of current-quarter changes in payrolls than of developments in the next quarter, to which it nominally relates.

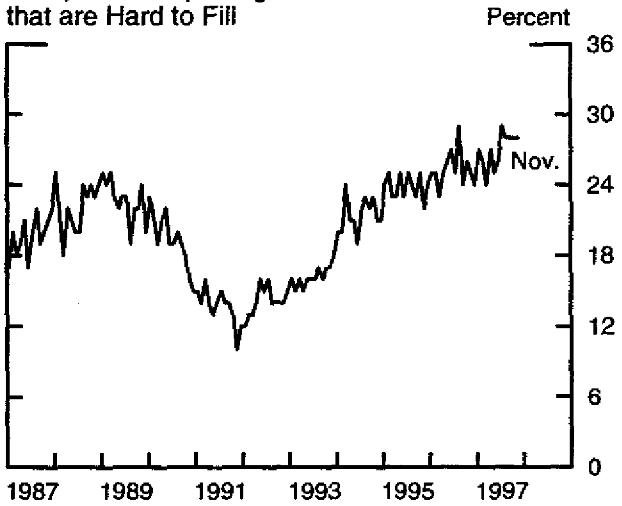
Labor Market Indicators

Initial Claims for Unemployment Insurance



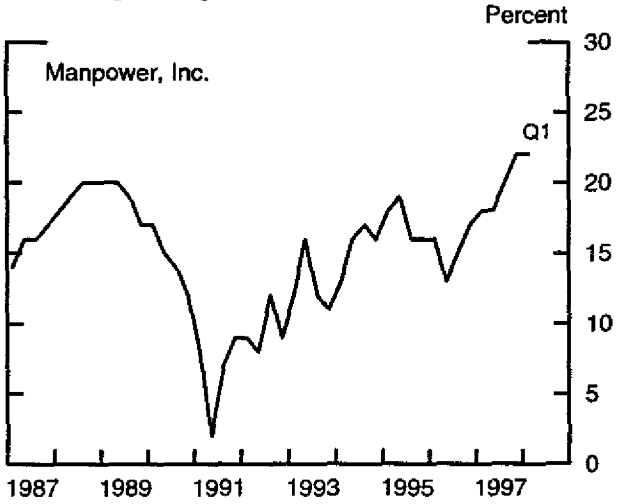
Note. State programs, includes EUC adjustment.

Companies Reporting Positions that are Hard to Fill



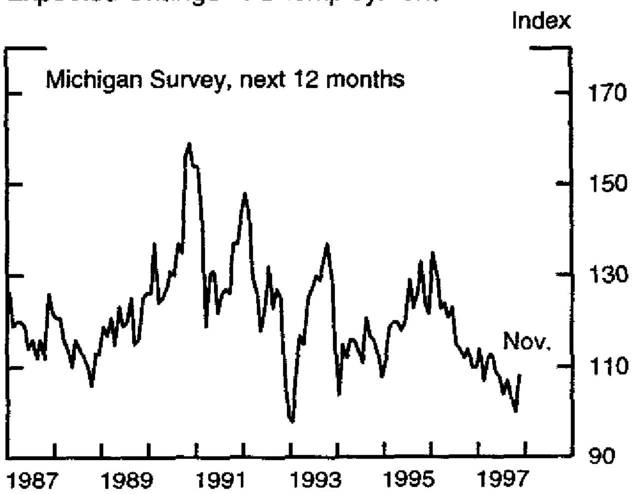
Source: National Federation of Independent Business.

Net Hiring Strength



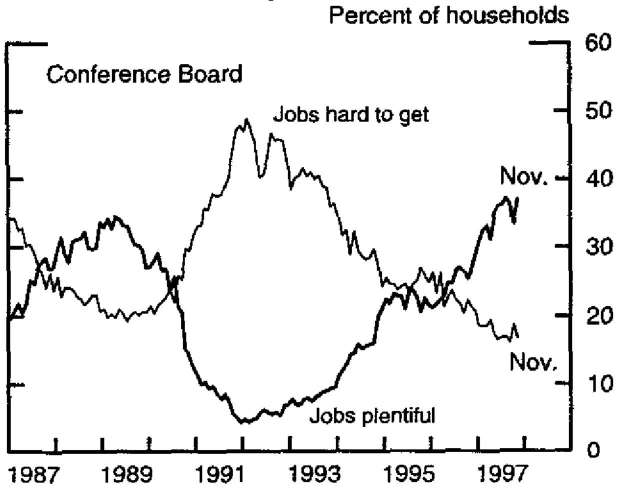
Note. Percent planning an increase in employment minus percent planning a reduction.

Expected Change in Unemployment



Note. Percentage expecting "more" minus percentage expecting "less" plus 100.

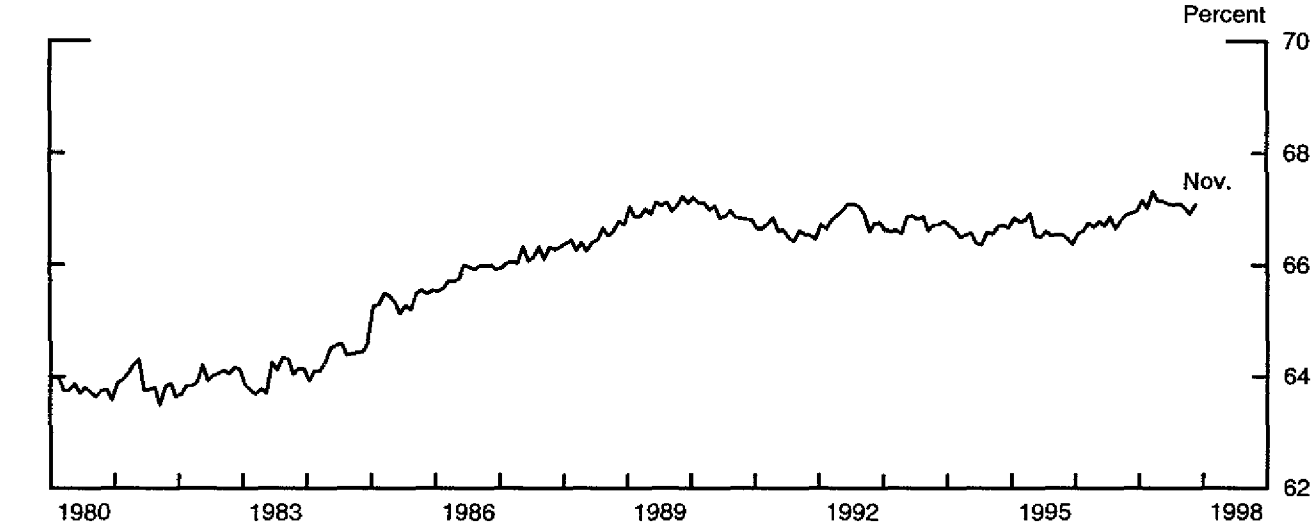
Current Job Availability



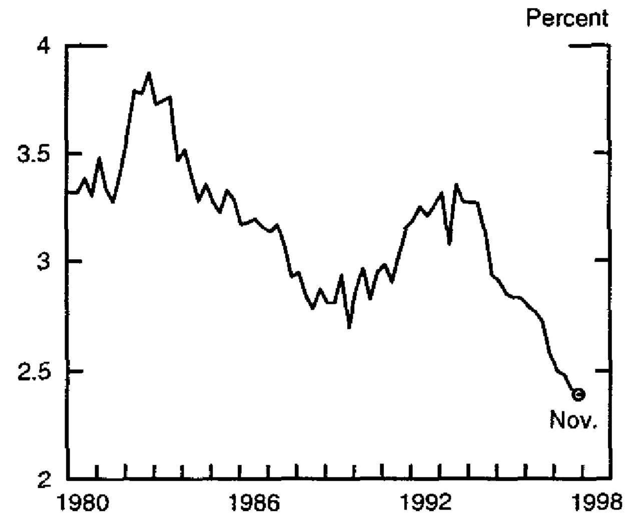
SELECTED UNEMPLOYMENT AND LABOR FORCE PARTICIPATION RATES
(Percent; based on seasonally adjusted data)

	1995	1996	1997 Q1	1997 Q2	1997 Q3	1997 Sept.	1997 Oct.	1997 Nov.
Civilian unemployment rate (16 years and older)	5.6	5.4	5.3	4.9	4.9	4.9	4.7	4.6
Teenagers	17.3	16.7	17.0	15.9	16.5	16.7	15.3	15.0
Men, 20 years and older	4.8	4.6	4.5	4.1	4.1	4.1	4.1	3.8
Women, 20 years and older	4.9	4.8	4.7	4.4	4.3	4.4	4.0	4.0
Labor force participation rate	66.6	66.8	67.2	67.1	67.1	67.0	66.9	67.1
Teenagers	53.5	52.3	52.6	51.8	50.9	50.7	50.6	52.1
Men, 20 years and older	76.7	76.8	77.0	77.0	76.9	76.8	76.8	77.0
Women, 20 years and older	59.4	59.9	60.4	60.5	60.6	60.6	60.4	60.3

Labor Force Participation Rate

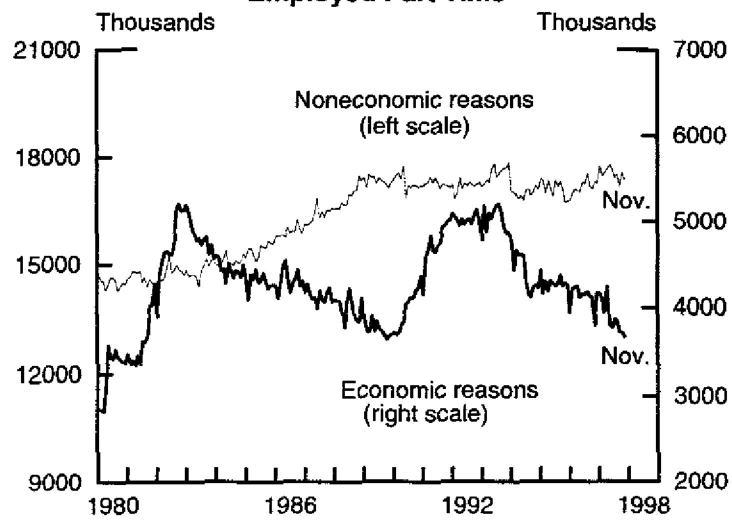


Percent of Population Not in the Labor Force Who Want Jobs



Note. Data are quarterly. Seasonally adjusted by FRB staff.

Employed Part Time



Note. Both series are adjusted for CPS redesign.

LABOR PRODUCTIVITY AND COSTS
(Percent change from preceding period at compound annual rate; based on seasonally adjusted data)

	1995 [1]	1996 [1]	1996 Q4	1997 Q1	1997 Q2	1997 Q3	1996:Q3 to 1997:Q3
Output per hour							
Total business	0.4	1.4	1.9	1.8	2.4	4.0	2.5
Nonfarm business	0.4	1.2	1.8	1.4	2.4	4.1	2.4
Manufacturing	3.3	3.9	3.7	2.5	2.8	9.3	4.6
Nonfinancial corporations [2]	1.4	2.2	2.0	1.9	2.5	6.7	3.3
Compensation per hour							
Total business	2.9	3.5	3.3	4.4	3.3	4.3	3.8
Nonfarm business	2.8	3.3	3.3	4.5	3.3	3.9	3.8
Manufacturing	3.3	3.1	1.9	4.4	2.6	3.4	3.1
Nonfinancial corporations [2]	2.6	3.2	2.9	4.3	3.3	4.5	3.8
Unit labor costs							
Total business	2.5	2.1	1.4	2.5	0.9	0.3	1.3
Nonfarm business	2.4	2.1	1.5	3.1	0.9	-0.2	1.3
Manufacturing	-0.1	-0.8	-1.7	1.8	-0.2	-5.4	-1.4
Nonfinancial corporations [2]	1.2	1.0	0.9	2.3	0.8	-2.1	0.5

1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.
2. Nonfinancial corporate sector includes all corporations doing business in the United States except banks, stock and commodity brokers, and finance and insurance companies; the sector accounts for about two-thirds of business employment.

AVERAGE HOURLY EARNINGS
(Percentage change; based on seasonally adjusted data)

	Twelve-month percent change [1] Nov. 1995	Nov. 1996	Nov. 1997	Percent change to Nov. 1997 May 1997	Aug. 1997	1997 Oct.	Nov.
	--- Annual rate ---			-Monthly rate-			
Total private nonfarm	2.8	3.6	4.3	4.6	5.3	0.4	0.6
Manufacturing	2.5	3.5	3.4	4.0	5.3	1.0	0.1
Durable	1.8	3.5	3.4	3.8	5.0	0.9	0.1
Nondurable	3.4	3.3	3.1	3.6	4.3	0.4	0.4
Construction	2.4	2.4	3.8	3.4	3.8	0.2	0.4
Transportation and public utilities	2.5	1.6	4.0	3.7	1.6	0.4	0.4
Finance, insurance, and real estate	4.2	3.9	5.5	6.9	4.2	0.5	0.7
Total trade	2.8	4.4	4.8	5.7	6.7	0.3	0.8
Retail trade	2.8	4.5	4.6	5.1	6.4	0.5	0.4
Wholesale trade	3.1	4.1	5.2	6.1	5.7	0.1	1.3
Services	3.3	4.1	4.5	5.0	5.6	0.4	0.7

1. Uses not seasonally adjusted data.

BLS to calculate output per hour.[2] Because hours for the self-employed and for unpaid family workers are so erratic, a productivity measure constructed using employee hours may provide a better signal of underlying productivity growth. By this measure, output per hour rose 2.3 percent at an annual rate in the third quarter. Although this figure is smaller than the standard BLS measure using the hours of all persons, it still represents a solid gain in productivity relative to its longer-run trend.

The hours of the self-employed and of unpaid family workers leapt 1.2 percent in November after falling 0.7 percent in October. Unless hours in this category surge in December, the net effect on the growth of total hours in the fourth quarter still will be somewhat negative, although much less so than last quarter. If hours in this category were to move back up further over the next few quarters, that rise would tend to damp the pace of productivity growth measured using the hours of all persons.

Compensation per hour in the nonfarm business sector rose at a 3.9 percent annual rate in the third quarter.[3] Over the past four quarters, compensation per hour grew 3.8 percent; this marks a 1 percentage point acceleration in hourly compensation over the past two years. However, the pickup in productivity growth has held unit labor costs in check; for the four quarters ended with 1997:Q3, unit labor costs grew only 1.3 percent.

Average hourly earnings provide the first reading of labor costs this quarter. In October and November, earnings rose 0.4 percent and 0.6 percent respectively. Over the past twelve months, average hourly earnings rose 4.3 percent, up from the 3.6 percent increase recorded over the previous twelve-month period. The jump in average hourly earnings in November may be exaggerated somewhat owing to some potential reporting problems the BLS has identified that tend to lead to relatively large increases in hourly earnings in months with fewer working days and small increases in

2. In the nonfarm business sector, the hours of the self-employed and of unpaid family workers fell 14 percent at an annual rate in the third quarter.

3. Compensation per hour is calculated using data on employee hours and, therefore, is not affected by swings in the growth of self-employed hours.

GROWTH IN SELECTED COMPONENTS OF INDUSTRIAL PRODUCTION
(Percent change from preceding comparable period)

	Proportion 1996	1996[1]	1997 H1	1997 Q3	1997 Aug.	1997 Sept.	1997 Oct.
			-Annual rate-		--Monthly rate---		
Total index	100.0	4.2	4.7	6.2	.5	.5	.4
Previous		3.9	4.4	6.6	.6	.5	.5
Manufacturing	86.2	4.7	5.4	6.1	.7	.2	.5
Durables	46.6	6.5	7.7	10.5	1.3	.4	.4
Motor vehicles and parts	5.2	-1.4	.5	20.6	6.8	1.6	-.8
Aircraft and parts	2.3	30.7	19.2	19.7	1.5	1.8	.9
Nondurables	39.6	2.5	2.7	1.2	.0	.1	.5
Manufacturing excluding motor vehicles and parts	81.0	5.1	5.7	5.3	.3	.2	.6
Mining	6.2	1.7	2.6	1.3	-.4	.2	-.8
Utilities	7.6	1.5	-.9	11.4	-.5	3.7	.3
IP by market group							
Consumer goods	28.3	2.4	1.6	3.0	.7	.0	.5
Durables	6.0	3.4	2.6	6.6	3.0	.0	.2
Nondurables	22.3	2.1	1.4	2.1	.1	.0	.6
Business equipment	13.7	8.2	8.6	13.6	2.2	-.2	.5
Information processing	5.5	11.8	10.5	15.7	1.0	.7	1.0
Industrial	4.5	.0	2.9	10.4	1.8	-1.0	.5
Transit	2.4	19.1	10.9	20.8	5.9	.5	-.7
Other	1.3	4.8	16.1	3.3	1.1	-1.9	.7
Construction supplies	5.6	5.8	3.4	-1.1	.9	-.6	-.1
Materials	40.3	4.7	6.1	8.7	.0	1.1	.4
Durables	22.9	6.7	9.1	12.5	.7	.9	.6
Semiconductors	3.7	25.5	40.9	42.6	2.5	2.1	2.2
Basic metals	3.6	3.2	2.9	4.3	.2	.5	.0
Nondurables	9.0	3.7	4.3	2.8	-1.0	.7	.4

1. From the final quarter of the previous period to the final quarter of the period indicated.

CAPACITY UTILIZATION
(Percent of capacity; seasonally adjusted)

	1988-89 High	1959-96 Avg.	1996 Q3	1997 Q2	1997 Q3	1997 Aug.	1997 Sept.	1997 Oct.
Manufacturing	85.7	81.7	81.5	81.5	81.6	81.8	81.6	81.7
Primary processing	88.9	82.8	85.9	86.0	85.8	85.8	85.8	85.8
Advanced processing	84.2	81.1	79.6	79.5	79.8	80.0	79.8	79.8

months with more.[4] That aside, the remaining acceleration looks to be not only a response to the jump in the minimum wage on September 1, but also some bidding up of wages in a tight labor market.

Industrial Production

Production worker hours and available physical product data suggest that industrial production rose sharply in November. A substantial increase in motor vehicle assemblies and related activity was one important component of November's advance. Production of information processing equipment and semiconductors appears again to have contributed significantly to the overall IP gain, whereas utilities output appears to have fallen following two strong months of growth.

Motor vehicle assemblies rose 5 percent in November; both auto and truck assemblies increased, together contributing about 0.1 percentage point to the rise in industrial production. Schedules for December call for production to drop to 12.2 million units at an annual rate.

Manufacturing production worker hours excluding motor vehicles and parts (FRB seasonals) rose 0.8 percent in November. Adding normal productivity gains and incorporating the available physical product data, output in manufacturing outside of the motor vehicles and parts sector likely soared in November. The increase in hours was widespread across industries; particularly notable were increases in industrial machinery and equipment, electrical equipment (including semiconductors), and food. Among industries

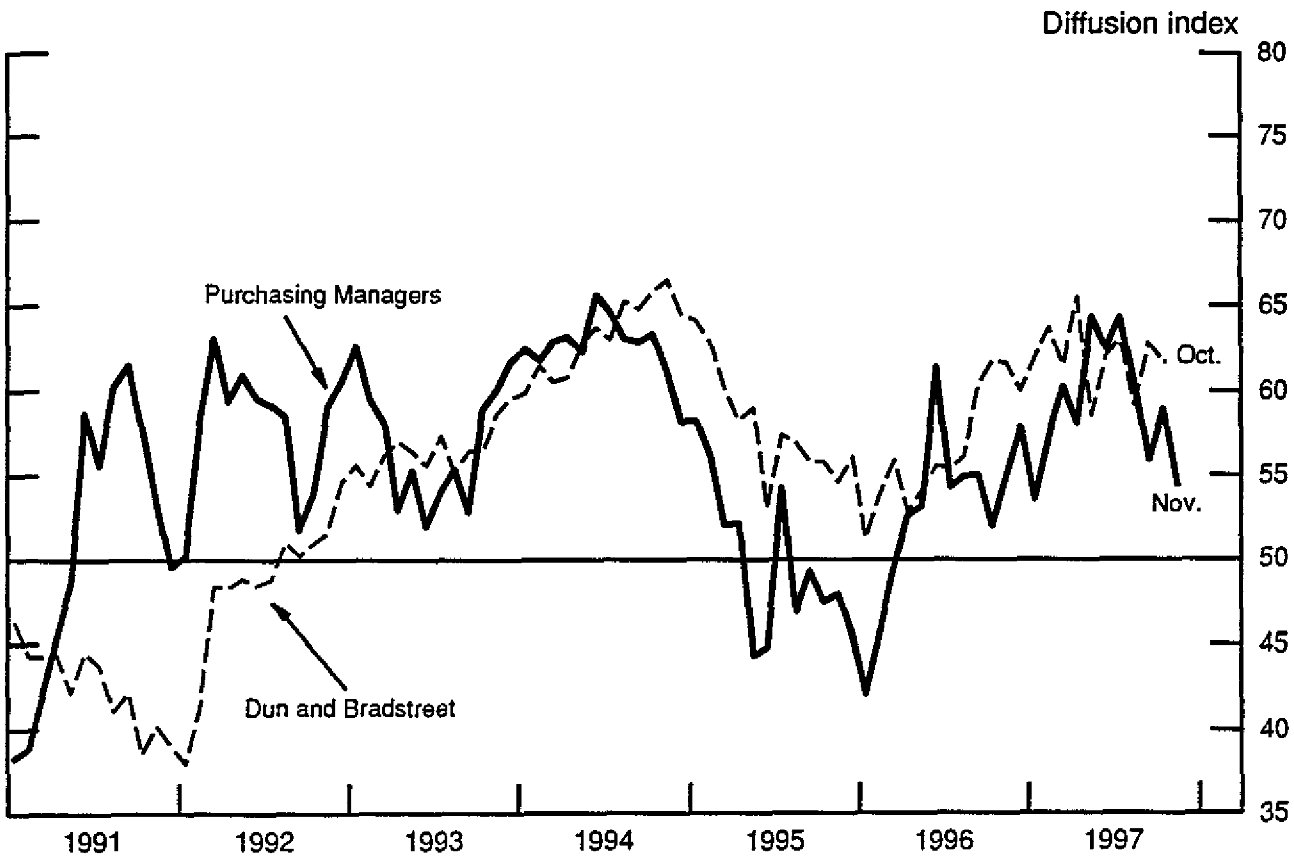
4. BLS has indicated that both the change in the workweek and average hourly earnings were biased upward in November by what are believed to be longstanding (although only recently discovered) difficulties in estimating weekly hours and payrolls for some establishments that pay their employees on a semimonthly or monthly basis. In particular, analysts there have identified a negative correlation between the number of working days in a month (which can range from 20 to 23 days) and the levels of average hourly earnings and the workweek. They are currently examining the microdata to ascertain the exact cause of this problem, but they currently suspect two likely sources of bias: (1) a tendency by some establishments to report the same number of hours regardless of the number of working days in the month; and (2) difficulties in distinguishing employees paid on an hourly basis from salaried nonsupervisory employees (who are treated differently in the processing of the monthly data). Because October had 23 working days and November had 20, we estimate that the correlation uncovered by the BLS caused the change in average hourly earnings to be overstated by roughly 0.3 percentage point. Because December has 23 working days, the change in average hourly earnings is likely to be depressed by a similar amount.

NEW ORDERS FOR DURABLE GOODS
(Percent change from preceding period, seasonally adjusted)

	Share, 1997:H1	1997 Q2	1997 Q3	1997 Aug.	1997 Sept.	1997 Oct.
Total durable goods	100.0	1.2	3.5	2.5	.0	-.1
Adjusted durable goods[1]	69.0	1.5	3.7	3.2	1.1	-2.0
Computers	5.0	.2	7.8	-2.2	3.4	-6.1
Nondefense capital goods excluding aircraft and computers	17.0	.4	7.0	-5.5	6.8	-3.1
Other	47.0	2,1	2.1	7.2	-1.1	-1.1
Memo:						
Real adjusted orders[2]		2.0	4.4	3.4	1.4	-2.2

1. Orders excluding defense capital goods, nondefense aircraft, and motor vehicle parts.
2. Nominal adjusted durable goods orders were split into two components, computers and all other. These components were deflated and then aggregated in a chain-weighted fashion.

Indicators of Future Production: New Orders Indexes



Note. Indexes above 50 indicate orders are increasing, and indexes below 50 indicate orders are decreasing.

for which weekly physical product data are available, appliances, steel, and lumber production showed small gains while petroleum refining fell in November.

PRODUCTION OF DOMESTIC AUTOS AND TRUCKS
(Millions of units at an annual rate; FRB seasonal basis)

	1997				
	Oct.	Nov.	Dec.	Q3	Q4
			Sched.		Sched.
U.S. production	12.4	13.0	12.2	11.9	12.5
Autos	5.9	6.1	5.8	6.0	5.9
Trucks	6.5	6.9	6.4	5.9	6.6
Days' supply					
Autos	61.2	63.6	--	56.8	--
Light trucks	74.4	68.9	--	71.9	--

Note. Components may not sum to totals because of rounding.

Production worker hours in the commercial aircraft industry (FRB seasonals) rose 2.4 percent in November, rebounding from October's 0.6 percent decline. October's falloff coincided with Boeing's shutdown of segments of the 747 production line because of parts shortages and other production difficulties. In November, the 747 line was brought back up, but the 737 production line was interrupted, also largely because of parts shortages. Both lines were up in early December, and Boeing plans to increase its assembly rate through the second quarter of next year.

Indicators of future production continue to point to a deceleration in IP in the months ahead: One important contibutor will be the scheduled slowdown in motor vehicle production. The staff's estimate of real adjusted durable goods orders fell 2.2 percent in October, but this decrease followed a very strong third quarter; on balance, the recent orders picture points to moderate growth in the near term. Both the National Association of Purchasing Managers and the Dun and Bradstreet Manufacturing Survey indexes of new orders are off a bit from earlier highs, but they remain at favorable levels.

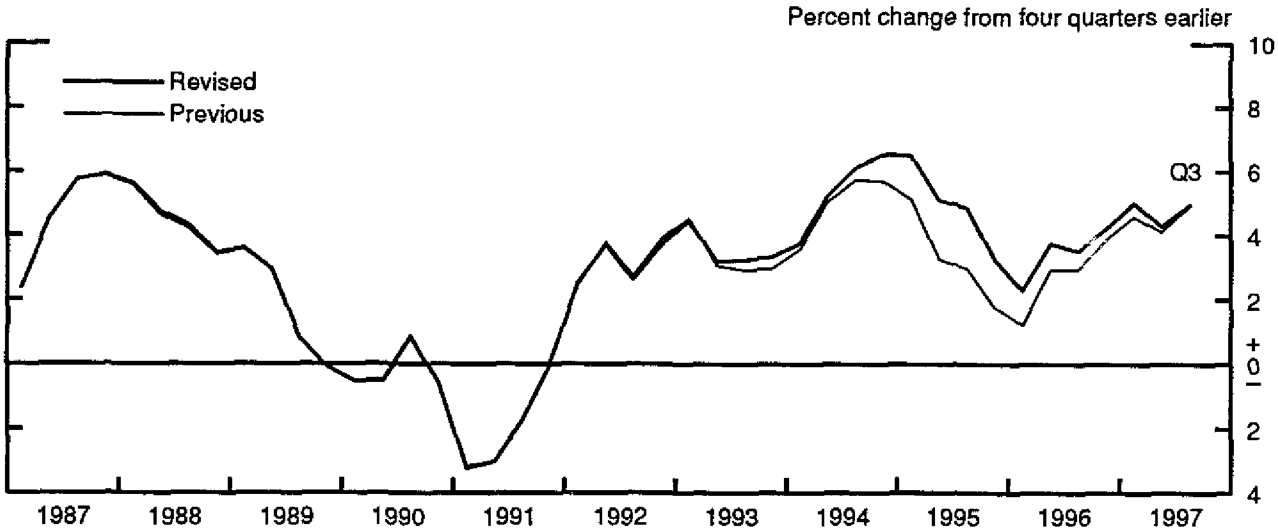
The staff recently published the annual revison of industrial production and capacity utilization. The revision incorporated information from the 1995 Annual Survey of Manufactures and the 1996 Survey of Plant Capacity, as well as updated monthly source data and new information on prices. The cumulative revision places the level of the production index in 1997:Q3 about 3 percent above the

Industrial Production and Capacity Utilization
1997:Q3

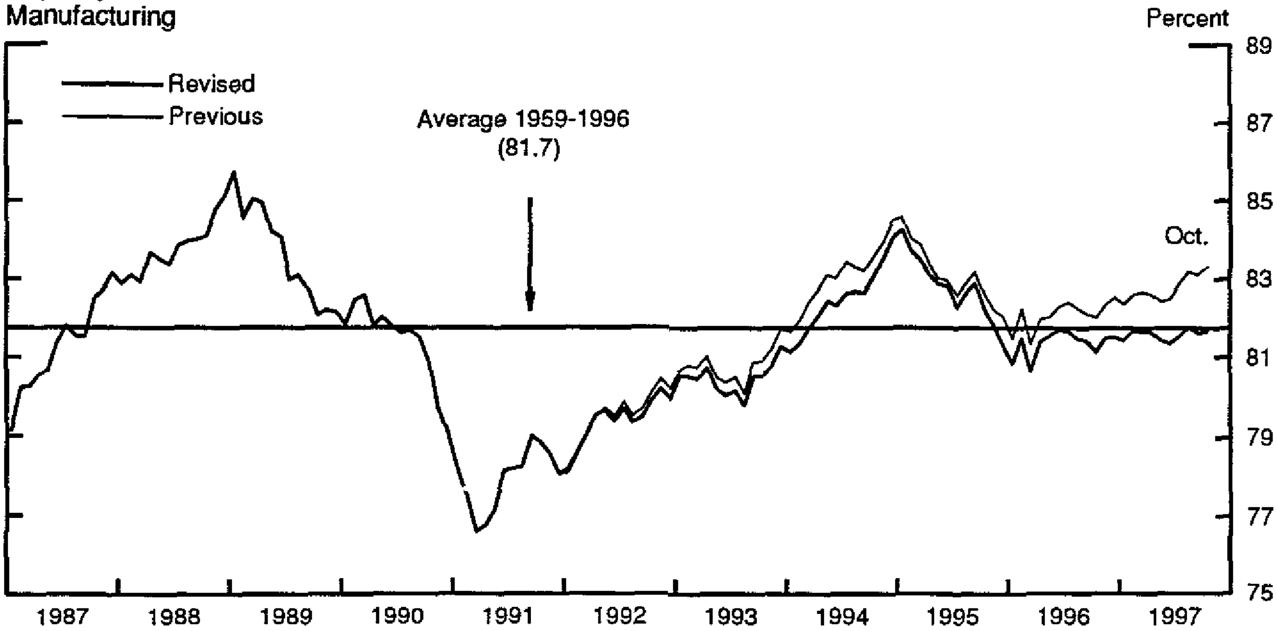
	Total Industry			Manufacturing
	Production[1]	Capacity[1]	Capacity Utilization	Capacity Utilization
1. Revised	125.2	151.3	82.7	81.6
2. *(Previous)*	*(121.5)*	*(144.6)*	*(84.0)*	*(83.1)*

1. Percent of output in 1992.

Industrial Production



Capacity Utilization
Manufacturing



previously published level for the third quarter. The largest upward revisions to growth were in 1994 and 1995. The index, nevertheless, continues to show some slowing in growth in the first half of 1995 after a surge in 1994. Growth still accelerates in 1996 and 1997, even though upward revisions averaged only about 1/4 percentage point in those years. The largest components of the upward revision came in the semiconductor and communications equipment industries, but output elsewhere, especially other durable manufacturing, was boosted as well.

Capacity utilization in manufacturing in the third quarter of this year was revised to 81.6 percent, 1-1/2 percentage points less than previously reported. The revised production indexes and information from the 1996 Survey of Plant Capacity, which provided industry utilization rates for the fourth quarters of 1995 and 1996, implied that manufacturing capacity growth was stronger than previously estimated. The revised annual rate of capacity growth in manufacturing exceeds 5 percent since 1995. Although a substantial portion of the upward revision in capacity growth occurred in the computer industry, the upward revision was not limited to high-technology industries.

With the revision, the utilization rate in manufacturing since 1995 has been at, or a bit below, its long-term average. Even more than the earlier figures, the revised ones show that an acceleration in the growth of capacity in recent years has accommodated this lengthy expansion without substantial pressures on manufacturers' productive capability.

Personal Income and Consumption

Total nominal retail sales turned up 0.2 percent in November, according to Census's advance report. Spending in the retail control category, which excludes sales at automotive dealers and at building material and supply stores, rose 0.3 percent last month; however, the similar-sized gains previously reported for September and October were cut in half. Nominal sales at apparel and at furniture and appliance stores turned up sharply in November, but sales at general merchandisers were little changed. This report, together with available information on prices, suggests that real PCE for goods excluding motor vehicles in October and November was about 0.2 percent higher than the average level in 1997:Q3 (not at an annual rate).

RETAIL SALES
(Percent change; seasonally adjusted)

	1997 Q2	1997 Q3	1997 Sept.	1997 Oct.	1997 Nov.
Total sales	-.8	1.8	-.3	-.2	.2
Previous estimate		1.9	-.1	-.2	
Building materials and supplies	1.7	-.7	-.1	1.0	-.8
Automotive dealers	-2.7	3.6	-1.6	-1.6	.2
Retail control[1]	-.4	1.4	.1	.2	.3
Previous estimate		1.5	.3	.4	
GAF	.3	1.9	-1.0	.5	.6
Durable goods	-.7	1.6	-.9	.8	.4
Furniture and appliances	2.1	1.9	-1.5	.0	1.3
Other durable goods	-2.8	1.4	-.5	1.4	-.2
Nondurables	-.3	1.4	.3	.1	.2
Apparel	-.2	2.8	-2.4	.1	1.2
Food	-.6	1.1	.8	.0	.4
General merchandise	-.2	1.5	-.3	.8	.1
Gasoline stations	-3.4	1.0	1.2	.5	-.5
Other nondurables	.9	1.4	.8	-.5	.1

1. Total retail sales less building material and supply stores and automotive dealers, except auto and home supply stores.

PERSONAL INCOME
(Average monthly percent change)

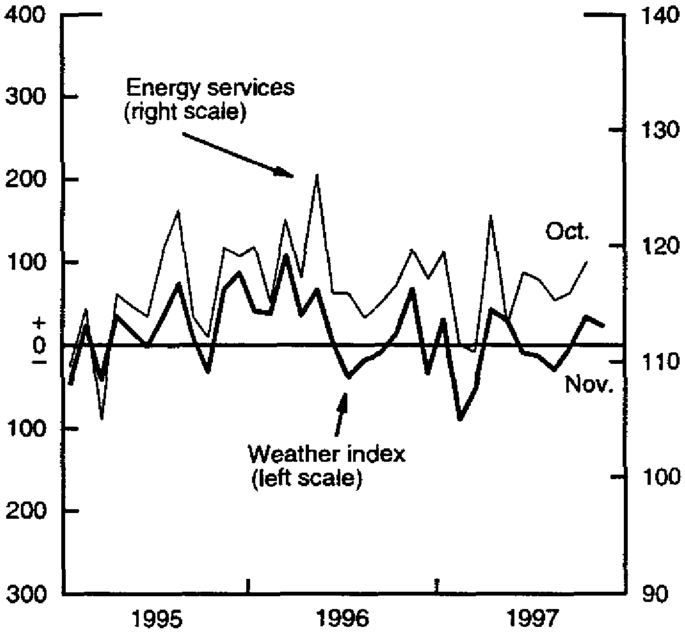
	1995	1996	1997 Q1	1997 Q2	1997 Q3	1997 Aug.	1997 Sept.	1997 Oct.
	-- Q4/Q4 --		--- Annual rate ---			--- Monthly rate ---		
Total personal income	5.2	5.8	8.0	5.0	4.7	.6	.3	.5
Wages and salaries	5.0	6.4	8.3	5.4	5.7	.8	.3	.6
Private	5.4	7.1	8.9	6.0	6.1	.9	.2	.7
Other labor income	-.9	.7	3.2	2.7	2.5	.2	.3	.3
Less: Personal tax and nontax payments	8.9	12.5	15.1	10.2	7.5	.8	.3	.6
Equals: Disposable personal income	4.7	4.8	6.8	4.2	4.3	.5	.3	.5
Memo:								
Real disposable income[1]	2.4	2.0	4.6	3.1	2.7	.4	.2	.3
Saving rate (percent)	4.8	4.3	3.7	4.2	3.5	3.6	3.6	3.6

Note. Derived from BEA's advance estimates.
1. Derived from billions of chained (1992) dollars.

Real PCE Services
(Percent change from the preceding period)

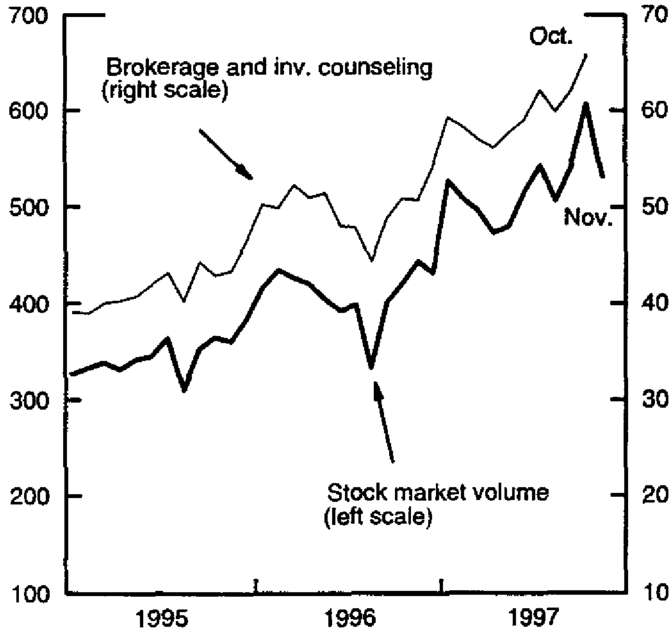
	1995	1996	1997 Q1	1997 Q2	1997 Q3	1997 Aug.	1997 Sept.	1997 Oct.
	— Q4/Q4 —		— Annual rate —			— Monthly rate —		
Services	2.7	2.8	3.9	3.9	4.1	.3	.3	.6
Energy	7.4	.7	−12.4	14.3	−5.5	−1.5	.6	2.2
Non–energy	2.4	2.9	4.7	3.4	4.5	.4	.3	.5
Housing	1.7	1.7	2.0	2.1	2.0	.2	.1	.2
Household operation	4.3	2.0	.3	5.4	8.2	.8	.4	.5
Transportation	4.9	4.2	4.8	3.3	5.9	.0	.7	.2
Medical	2.2	2.5	4.2	2.5	4.4	.5	.3	.4
Personal business	1.6	4.6	8.5	3.6	6.3	.0	.6	1.1
Other	3.0	4.1	8.1	6.1	5.3	.7	−.2	.6

Energy Services



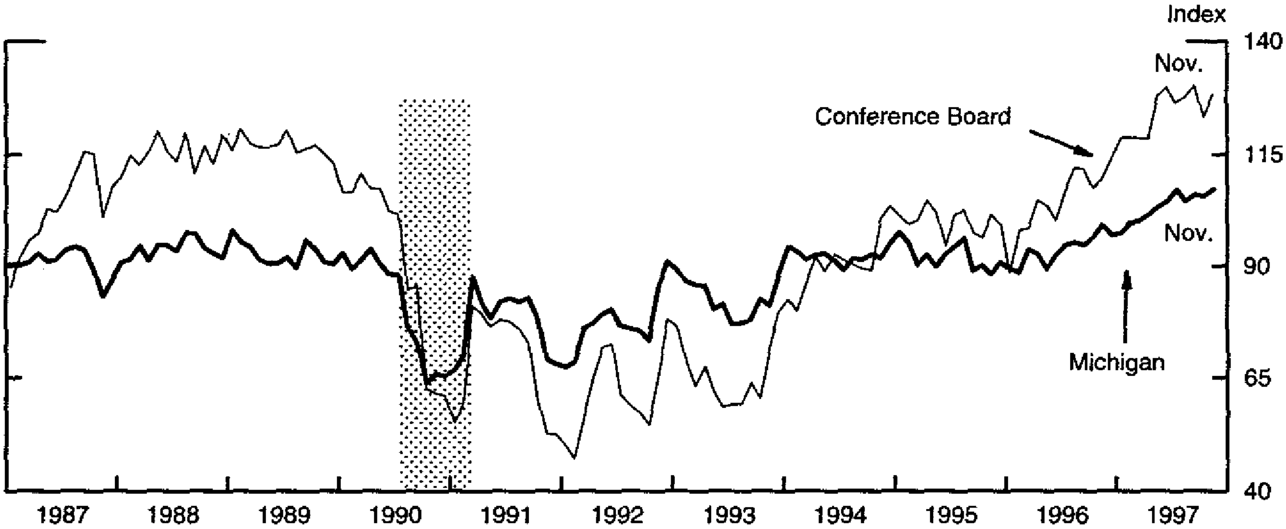
Note. The weather index is the deviation in the number of heating and cooling degree days in a month from that month's average over the past five years.

Brokerage Services

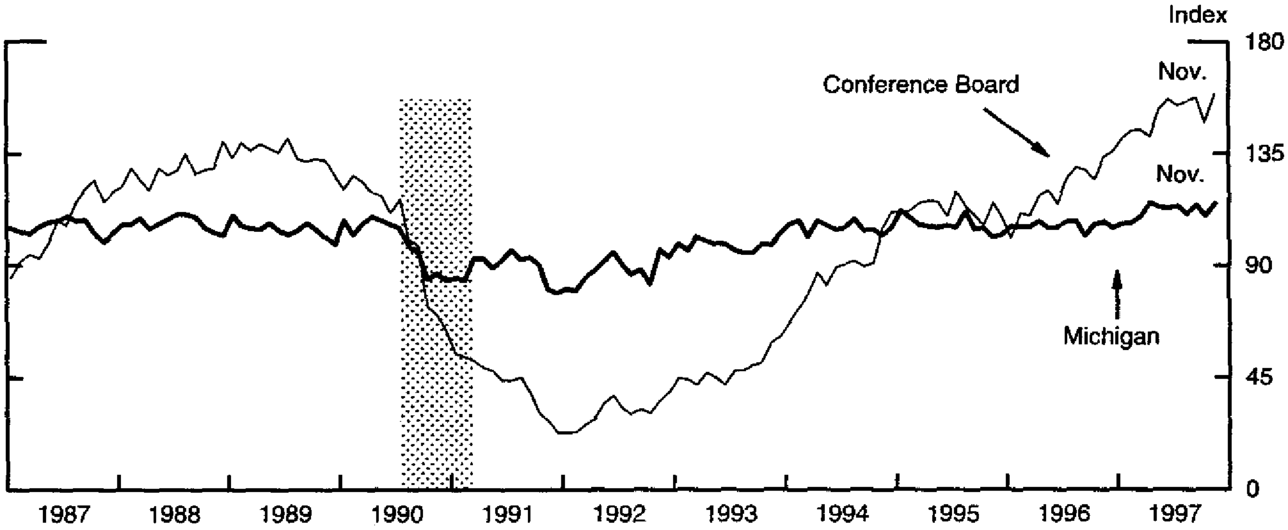


Consumer Surveys

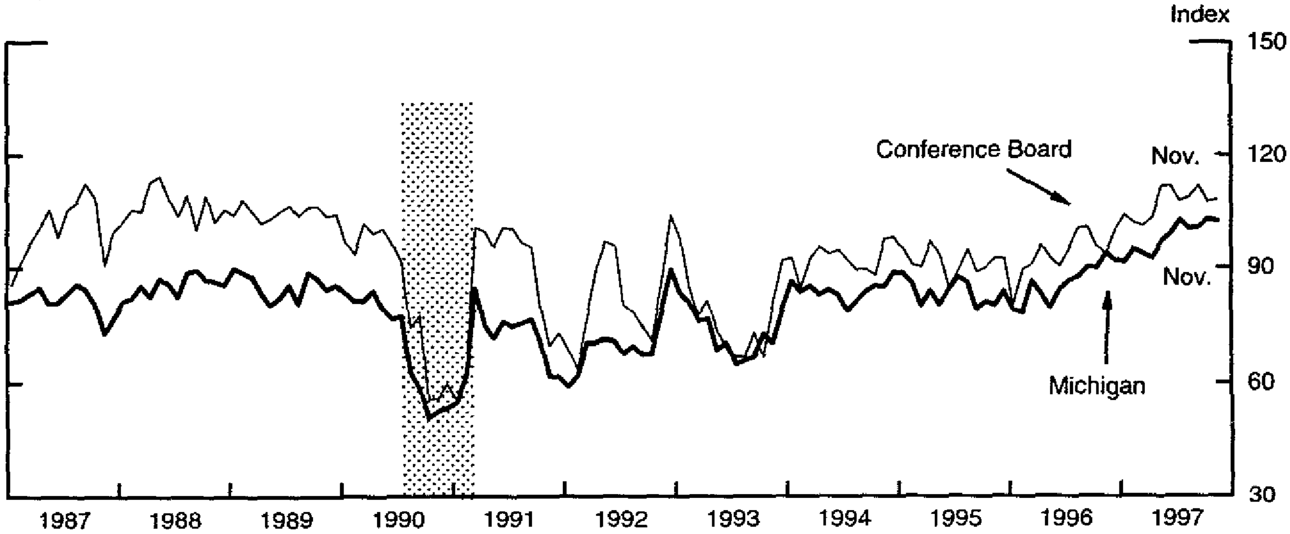
Consumer Sentiment



Current Conditions



Expected Conditions



Real spending on services rose 0.6 percent in October, the latest month for which data are available. Expenditures on energy services jumped 2.2 percent in October (on a seasonally adjusted basis), as temperatures returned to normal after a relatively warm September. According to national weather data, temperatures in November ran a bit below normal, pointing to another rise in energy spending last month. Outlays for non-energy services increased 0.5 percent in October, boosted by a surge in expenditures on brokerage services and solid gains in spending in other categories. Trading volumes on major U.S. exchanges--an indicator used by the BEA when constructing its monthly estimates of PCE for brokerage services--dropped back in November, making a decline in spending on brokerage services that month highly likely.

Estimates of personal income are available only through October. In that month, real disposable personal income rose 0.3 percent, boosted by a hefty gain in private wage and salary disbursements. Aggregate hours worked and average hourly earnings (even after adjusting for reporting problems) made substantial gains in November, suggesting that private wage and salary disbursements will show another large increase for the month.

Readings of consumer sentiment for November continued to show that households have euphoric views of economic conditions. The Michigan index rose to a historical high in November, while the Conference Board index climbed back to the upper end of the very favorable range that has prevailed since last May. In both the Michigan and Conference Board surveys, respondents' views of current conditions improved in November, while appraisals of expected conditions held steady. On balance, the strong economic outlook as seen from Main Street seemed to be unaffected by the recent turbulence on Wall Street and in financial markets abroad: In last month's Michigan survey, respondents reported more favorable views of their personal financial situations and of buying conditions for large household items, and in the Conference Board survey, respondents' appraisals of current job availability and current business conditions strengthened further last month.

Motor Vehicles

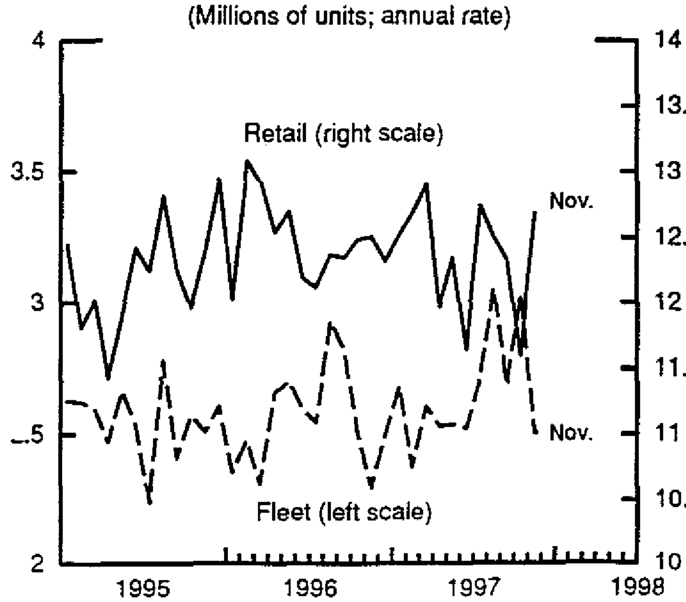
Adjusted for shifts in reporting periods, sales of new light motor vehicles rose to 15.1 million units (annual rate) in November, more than retracing the dip in sales in October. Sales at the Big Three rose 500,000 units, accounting for nearly all of the increase.

SALES OF AUTOMOBILES AND LIGHT TRUCKS
(Millions of units at an annual rate; FRB seasonals)

			1997			1997		
	1995	1996	Q1	Q2	Q3	Sept.	Oct.	Nov.
Total	14.7	15.1	15.3	14.5	15.3	15.0	14.6	15.2
Adjusted[1]	14.7	15.0	15.2	14.7	15.3	15.6	14.6	15.1
Autos	8.6	8.5	8.5	8.0	8.4	8.2	7.9	7.9
Light trucks	6.1	6.6	6.7	6.5	6.9	6.9	6.7	7.3
North American[2]	12.8	13.4	13.3	12.7	13.3	13.0	12.7	13.3
Autos	7.1	7.3	7.2	6.7	7.0	6.8	6.6	6.5
Big Three	5.4	5.3	5.1	4.8	5.1	5.1	4.8	4.6
Transplants	1.7	2.0	2.1	1.9	2.0	1.7	1.8	1.9
Light trucks	5.7	6.1	6.2	5.9	6.3	6.3	6.1	6.8
Foreign produced	1.9	1.7	1.9	1.8	2.0	2.0	1.9	1.9
Autos	1.5	1.3	1.4	1.3	1.4	1.4	1.3	1.3
Light trucks	.4	.4	.5	.6	.6	.6	.6	.5

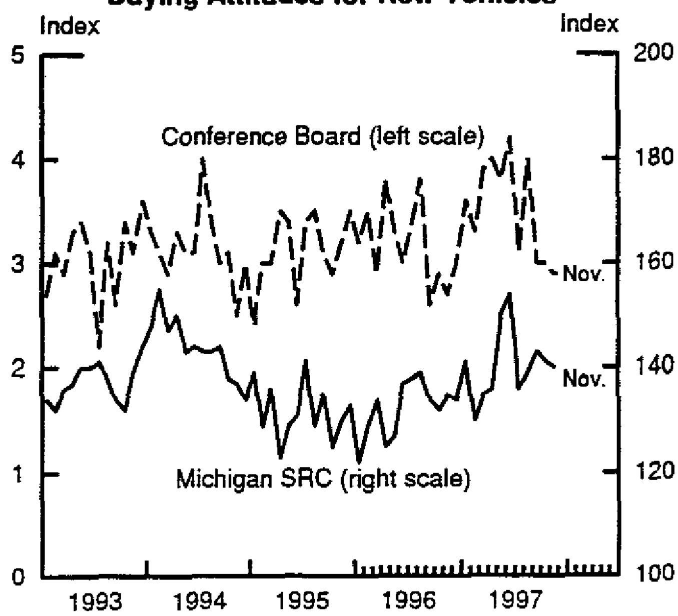
Note. Components may not sum to totals because of rounding. Data on sales of trucks and imported autos for the most recent month are preliminary.
1. Excludes the estimated effect of automakers' changes in reporting periods.
2. Excludes some vehicles produced in Canada that the industry classifies as imports

Total Industry Fleet and Retail Sales
(Millions of units; annual rate)



Note. FRB staff estimate

Buying Attitudes for New Vehicles



The improvement appears to have been the result of increased deliveries to consumers; confidential company data from both GM and Ford indicate that their fleet sales declined last month. A source at GM also reported that delays in rail deliveries were no longer a factor holding down sales in November.

Several factors are working to sustain healthy sales of motor vehicles to consumers. In November, attitudes regarding car-buying conditions remained in the middle of the favorable range seen over the past year, according to the Michigan SRC survey. The November reading on buying plans from the Conference Board ticked down but is still at a level consistent with a solid sales pace. In part, these opinions have been bolstered by the competitive pricing among major producers. Sales incentives are still sizable and are expected to remain high over the near term. Despite solid sales, Toyota has put in place modest incentives to ensure that the Camry does not lose its number 1 sales position to the new Honda Accord.

Housing Markets

The housing sector has remained strong in the fourth quarter. Housing starts rose to 1.53 million units (annual rate) in October, as a sharp rise in multifamily construction outweighed a decline in single-family starts.

Although starts of single-family units fell back after having reached a high level in September, the October pace of 1.14 million units was equal to the third-quarter average. Adjusted permit issuance for single-family units strengthened in October to a level that suggests that the starts figure may understate the pace of construction activity.

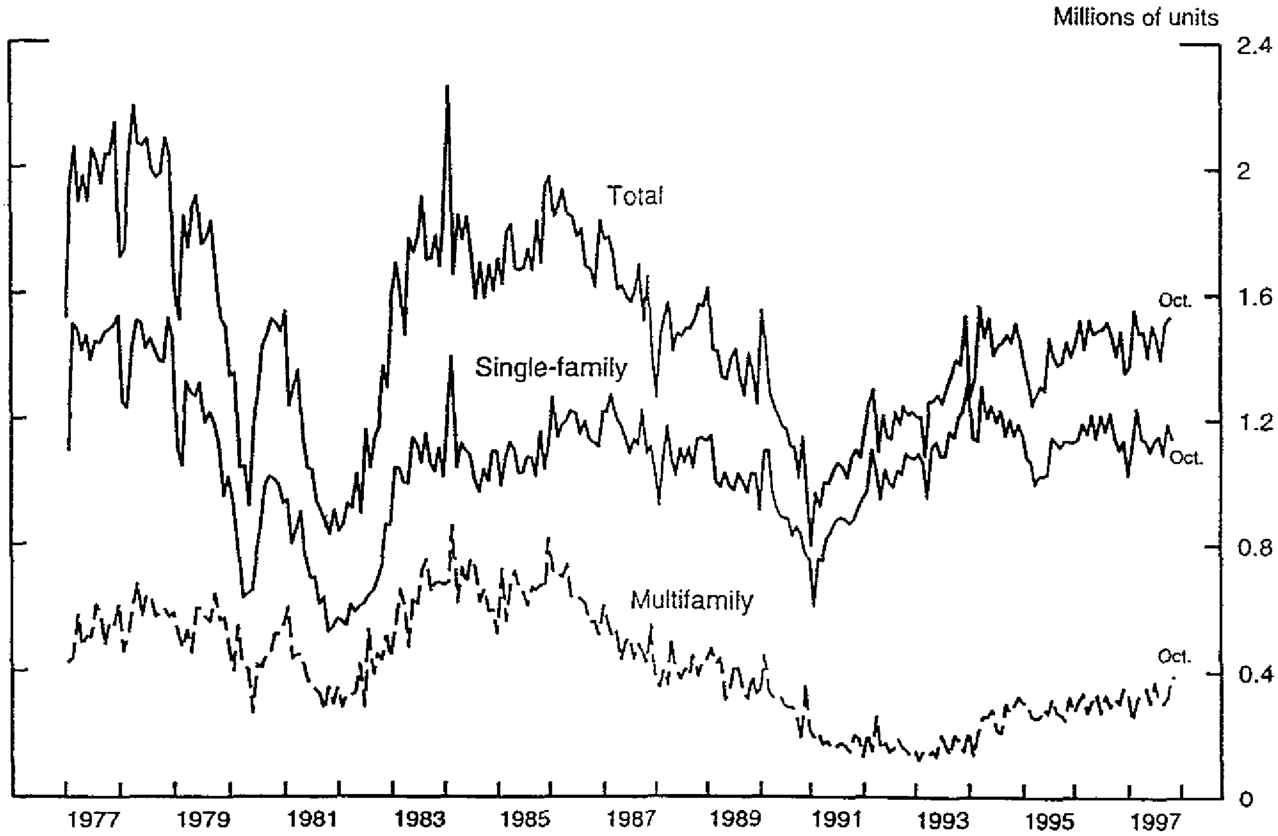
The fundamentals of demand for single-family housing have shown continued strength in recent months: Gains in employment and income have remained sizable, and mortgage rates have declined further. Although sales of new homes slipped a bit in October, they remained high, and homebuilders' ratings of new home sales remained quite positive through early November. Existing home sales, which (because they are recorded predominantly at the closing rather than at the signing of the contract) respond to changing market conditions somewhat less rapidly than new home sales, rose in October to another high for the series. The SRC index of consumer attitudes toward homebuying conditions, when adjusted for seasonal variation, increased in November to the most favorable reading in three and one-half years. Applications for mortgages to finance

Private Housing Activity
(Millions of units; seasonally adjusted annual rate)

	1996	1997 Q1	1997 Q2	1997 Q3r	1997 Aug.r	1997 Sept.r	1997 Oct.p
All units							
Starts	1.48	1.47	1.46	1.46	1.40	1.51	1.53
Permits	1.43	1.43	1.43	1.42	1.40	1.46	1.49
Single-family units							
Starts	1.16	1.17	1.12	1.14	1.09	1.19	1.14
Permits	1.07	1.05	1.05	1.04	1.03	1.07	1.09
New home sales	.76	.82	.78	.81	.79	.81	.80
Existing home sales	4.09	4.10	4.15	4.27	4.31	4.31	4.40
Multifamily units							
Starts	.32	.30	.34	.31	.30	.32	.39
Permits	.36	.38	.37	.38	.37	.40	.40
Mobile homes							
Shipments	.36	.35	.36	.36	.36	.37	n.a.

Note. p Preliminary. r Revised. n.a. Not available.

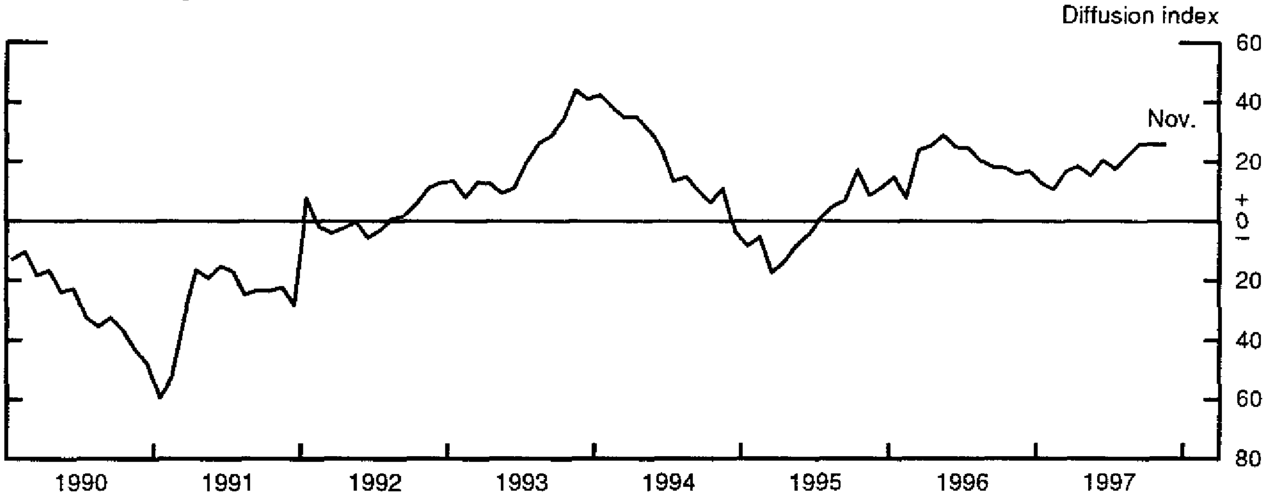
Private Housing Starts
(Seasonally adjusted annual rate)



Indicators of Housing Demand

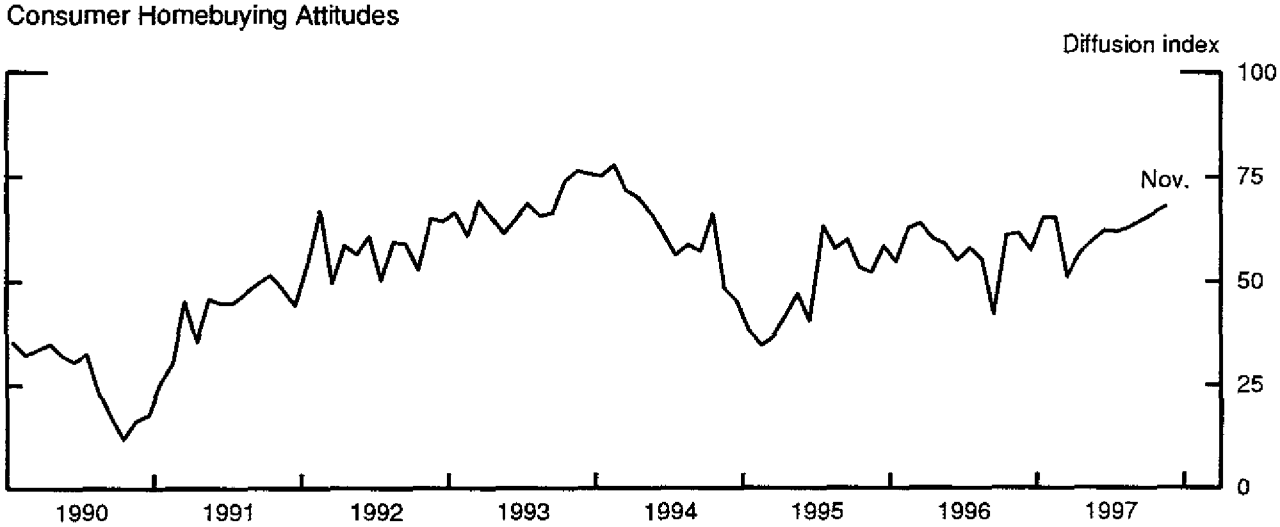
(Seasonally adjusted; FRB seasonals)

Builders' Rating of New Home Sales



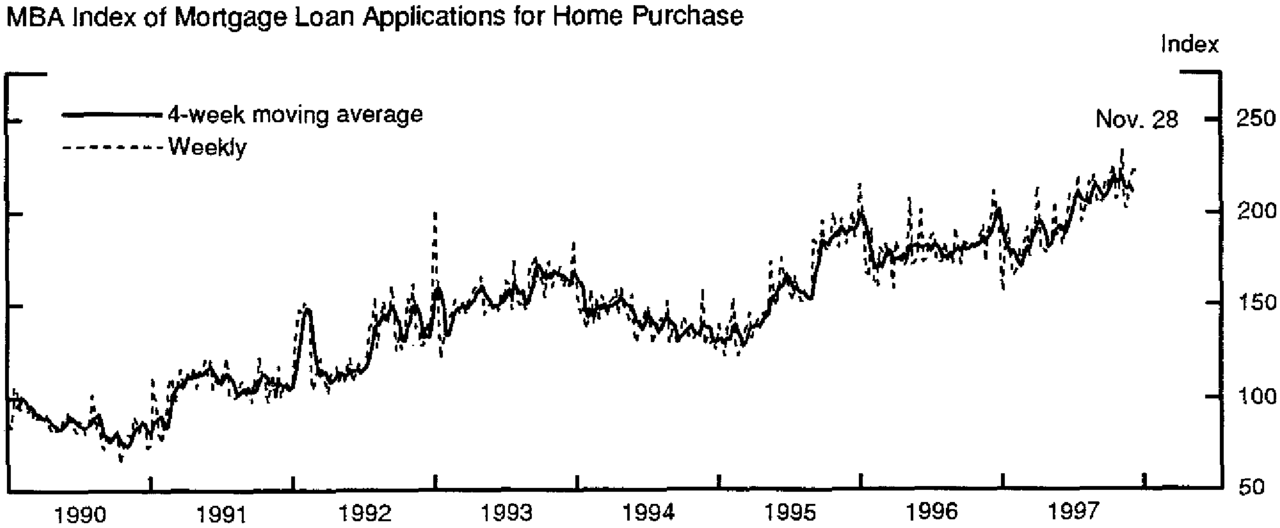
Note. The index is calculated from National Association of Homebuilders data as the proportion of respondents rating current sales as good minus the proportion rating them as poor.

Consumer Homebuying Attitudes



Note. The homebuying attitudes index is calculated from Survey Research Center data as the proportion of respondents rating current conditions as good minus the proportion rating conditions as bad.

MBA Index of Mortgage Loan Applications for Home Purchase



BUSINESS CAPITAL SPENDING INDICATORS
(Percent change from preceding comparable period;
based on seasonally adjusted data, in current dollars)

	1997		1997		
	Q2	Q3	Aug.	Sept.	Oct.
Producers' durable equipment					
Shipments of nondefense capital goods	5.5	3.9	-2.4	3.4	-2.3
Excluding aircraft and parts	4.1	4.0	-1.2	3.2	-.9
Office and computing	2.3	5.5	-1.6	1.6	-1.8
Communications equipment	6.2	7.8	3.8	-2.5	.1
All other categories	4.3	2.6	-2.3	5.3	-.9
Shipments of complete aircraft[1]	24.0	12.7	-31.9	31.3	-14.4
Sales of heavy trucks	-1.8	4.7	-8.0	3.6	5.6
Orders of nondefense capital goods	-.5	6.5	1.2	1.3	1.4
Excluding aircraft and parts	.3	7.2	-4.8	6.1	-3.8
Office and computing	.2	7.8	-2.2	3.4	-6.1
Communications equipment	4.6	-.6	6.8	4.8	-8.8
All other categories	-.7	9.1	-8.4	7.4	-1.6
Nonresidential structures					
Construction put in place, buildings	-2.0	3.2	-.9	-.5	-1.1
Office	-3.3	8.9	-.2	1.0	1.7
Other commercial	-5.8	.6	-2.1	-5.5	.1
Institutional	4.6	.8	2.4	5.6	-.1
Industrial	-3.9	4.2	-1.4	-.9	-5.0
Lodging and miscellaneous	3.5	2.8	-2.3	1.3	-3.8
Rotary drilling rigs in use[2]	11.9	-3.5	-1.4	-2.4	-3.4
Memo:					
Business fixed investment	14.6	18.1	n.a.	n.a.	n.a.
Producers' durable equipment	23.0	24.1	n.a.	n.a.	n.a.
Office and computing	46.2	48.2	n.a.	n.a.	n.a.
Communications equipment	7.9	33.8	n.a.	n.a.	n.a.
Other equipment[3]	19.7	9.3	n.a.	n.a.	n.a.
Nonresidential structures	-4.7	3.3	n.a.	n.a.	n.a.

1. From the Current Industrial Report "Civil Aircraft and Aircraft Engines." Monthly data are seasonally adjusted using FRB seasonal factors constrained to BEA quarterly seasonal factors. Quarterly data are seasonally adjusted using BEA seasonal factors.
2. Percent change of number of rigs in use, seasonally adjusted.
3. Producers' durable equipment excluding office and computing, communications, motor vehicles, and aircraft and parts.
n.a. Not available.

home purchases have risen to the highest point in the eight-year history of the series.

Multifamily housing starts soared in October to 386,000 units, which is the highest monthly estimate in nearly eight years. However, permit issuance for multifamily structures was little changed, raising doubts about the sustainability of this high level of starts. The vacancy rate for multifamily rental units in the third quarter was below its year-earlier level for the fourth consecutive quarter, indicating that the vacant stock is diminishing slowly even though, at 9.2 percent, it remains relatively high.

Business Fixed Investment

Growth of real business fixed investment appears to be moderating from the torrid pace registered in the second and third quarters. Nonetheless, investment fundamentals appear to be strong: Business output growth has been robust, corporate cash flow is healthy, and the real user cost-of-capital--especially for computing equipment--remains low.

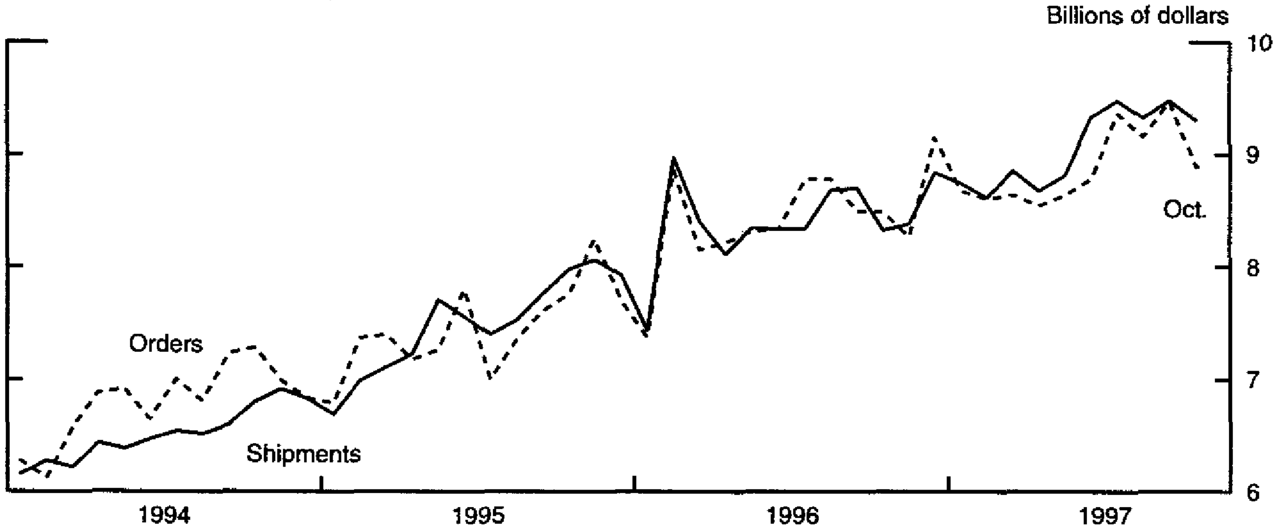
Nominal shipments of office and computing equipment fell 1.8 percent in October but remained at a high level. With prices of personal computers continuing to fall rapidly, real spending on office and computing equipment ought to post a solid gain in the fourth quarter. Notably, Intel recently announced a restructuring of its microprocessor business to better enable it to reduce costs and match the prices charged by its competitors. The lukewarm acceptance in the marketplace of the top-of-the-line Pentium II chip also makes price reductions likely.

Shipments of communications equipment edged up in October after posting strong gains in the third quarter. This sector has grown rapidly this year, as Internet usage and telecommunications deregulation have led to the expansion of local phone networks. Moreover, price declines are expected this quarter, pointing to a healthy gain in real outlays.

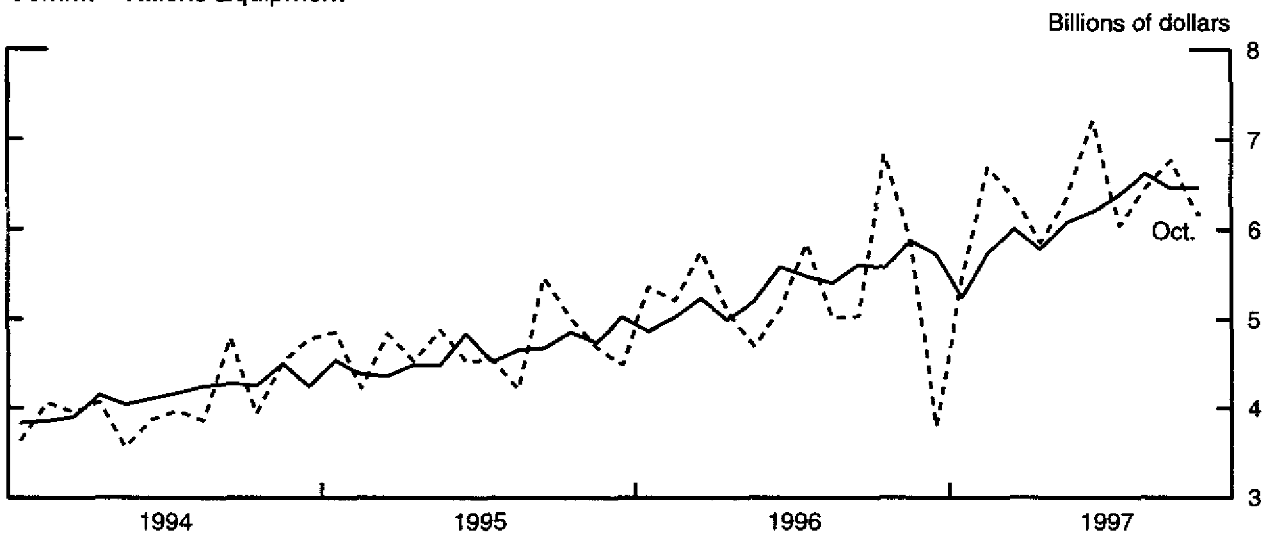
In contrast to the high-tech sector, expenditures on transportation equipment appear likely to be a drag on producers' durable equipment in the fourth quarter. Real domestic spending on aircraft is likely to fall in the fourth quarter because of production disruptions at Boeing. Business demand for heavy trucks was exceptionally robust in October, when sales surged to 454,000 units (annual rate)--noticeably above the strong third-quarter pace--and sales in November remained close to that high level.

Orders and Shipments of Nondefense Capital Goods

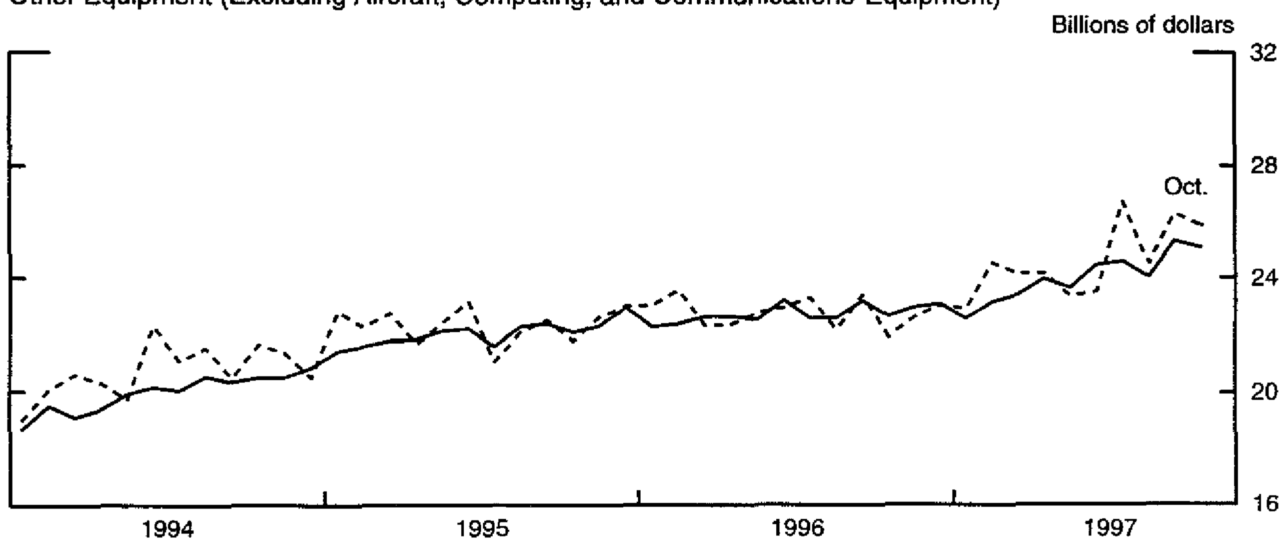
Office and Computing Equipment



Communications Equipment



Other Equipment (Excluding Aircraft, Computing, and Communications Equipment)



However, with fleet sales of light motor vehicles in October and November below their third-quarter rate, overall business spending on vehicles is likely to decline this quarter.

New orders for nondefense capital goods excluding aircraft and high-tech equipment fell 1.6 percent in October, but they continue to run well ahead of shipments. Shipments in this category fell 0.9 percent in October. Much of the drop was driven by a sharp decline in shipments of railroad equipment, which tend to be highly erratic. Excluding railroad equipment, shipments in this category fell 0.2 percent.

Spending on nonresidential structures is on track to end the year lower than it started, despite some strong fundamentals. Commercial real estate prices, as indicated by the National Real Estate Price Index, have continued to move up this year, while vacancy rates have fallen because of robust demand for space. The FDIC real estate survey of senior examiners and asset managers also reports a very upbeat assessment of the strength of the commercial market. Nonetheless, private nonresidential construction put-in-place fell 1.1 percent in October after having declined 0.5 percent in September. These data, coupled with information on construction contracts, point to a decrease in outlays on structures in the current quarter.

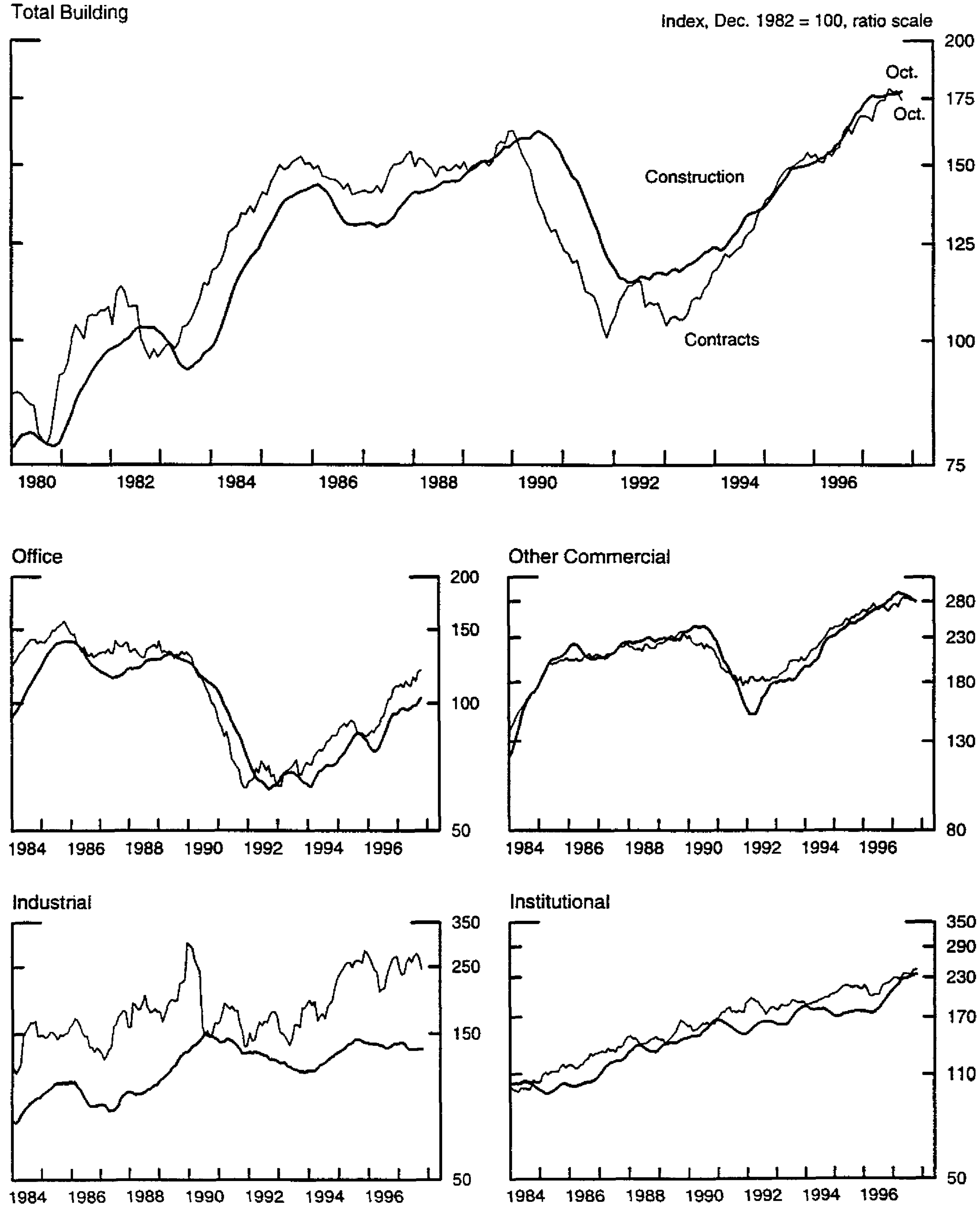
Business Inventories

On a book-value basis, manufacturers' inventories increased at a $24 billion annual rate in October, a touch faster than the average rate for the third quarter. With shipments declining 0.1 percent, the inventory-shipments ratio for all manufacturing ticked up to 1.35 months, the same as its average value for the third quarter.

Inventories of durable goods increased at a $10 billion annual rate in October, boosted by another large increase in stocks of aircraft and parts, which were up $6 billion (annual rate). The inventory-shipments ratio for aircraft and parts rose sharply, to 4.7, an increase most likely associated with Boeing's recent difficulties in completing aircraft. Inventories of nondurable goods increased at a $14 billion annual rate in October, driven by another large buildup in inventories of chemicals, which expanded at a $7 billion annual rate. Shipments of nondurable goods advanced 0.8 percent in October, keeping the inventory-sales ratio flat at 1.12 months.

Nonresidential Construction and Contracts

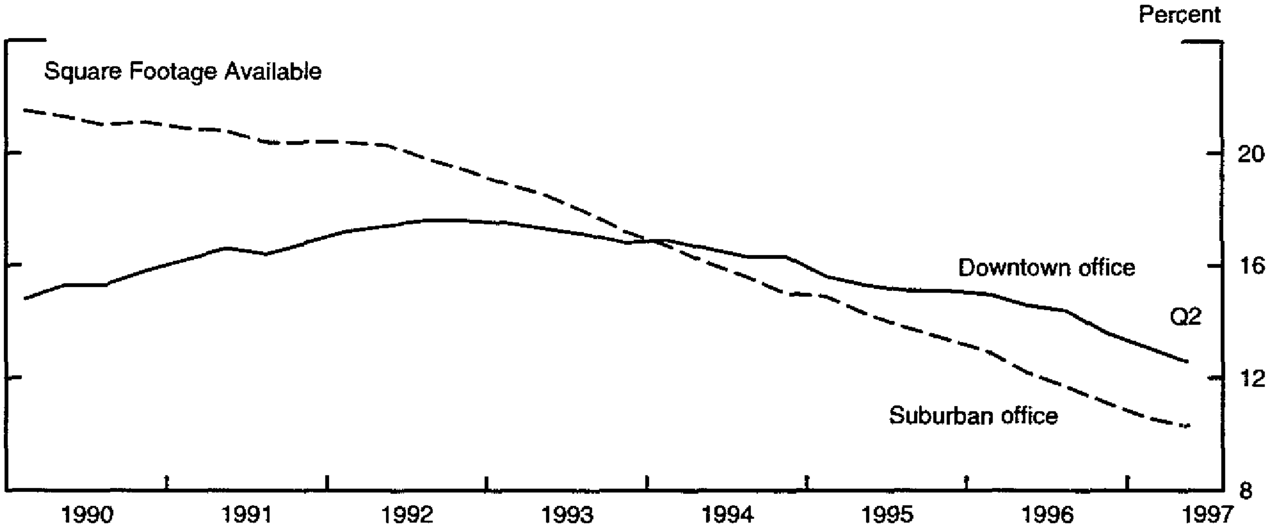
(Six-month moving average)



Note. For contracts, total includes private only; individual sectors include public and private.

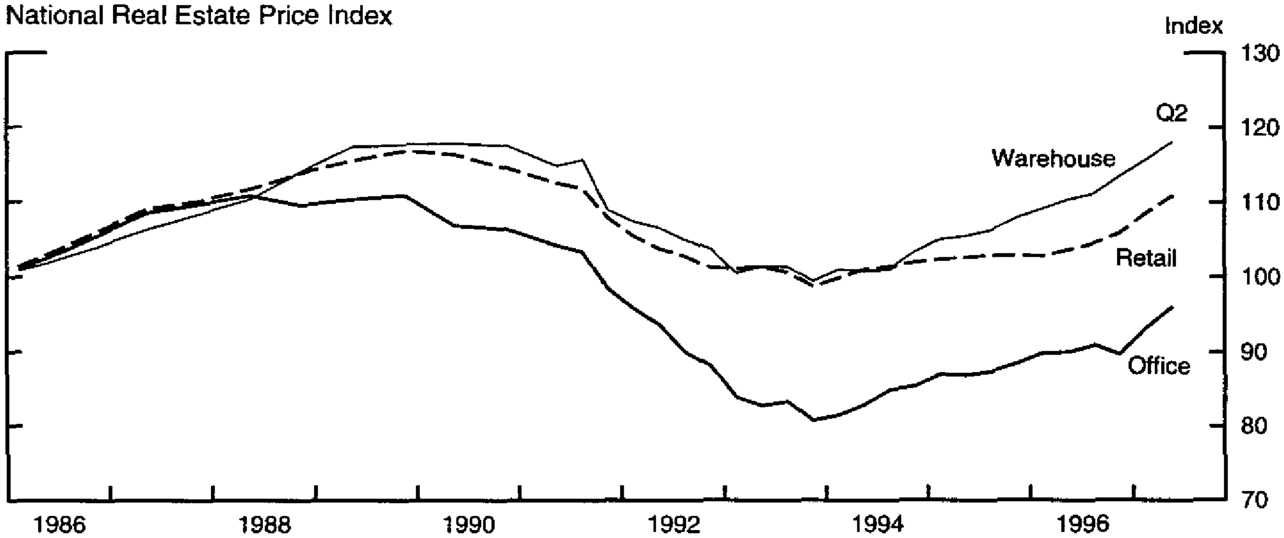
Nonresidential Construction Indicators

Vacancy Rates



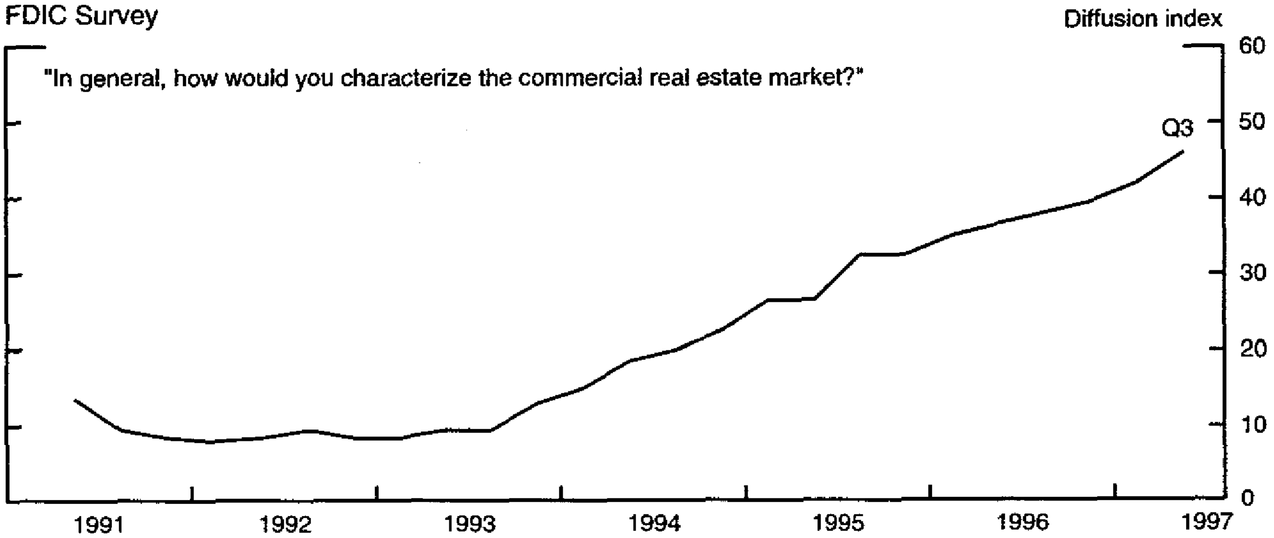
Source: CB Commercial Real Estate

National Real Estate Price Index



Note. Data are semiannual from 1986 to 1991 and quarterly from 1992 forward

FDIC Survey



Note. Calculated as [(Percent reporting tight supply - Percent reporting excess supply)/2] + 50.

CHANGES IN MANUFACTURING AND TRADE INVENTORIES
(Billions of dollars at annual rates;
based on seasonally adjusted data)

	1997			1997		
	Q1	Q2	Q3	Aug.	Sept.	Oct.
Book value basis						
Total	35.8	51.5	44.9	29.5	87.0	n.a.
Excluding wholesale and retail motor vehicles	30.9	48.9	36.8	21.1	71.7	n.a.
Manufacturing	16.5	25.1	17.3	22.1	8.5	23.9
Excluding aircraft	9.1	19.8	13.3	12.0	11.9	18.1
Wholesale	14.3	19.1	15.8	31.0	38.6	18.5
Excluding motor vehicles	11.5	14.3	14.2	25.5	34.1	21.3
Retail	5.0	7.4	11.8	-23.7	39.9	n.a.
Auto dealers	2.1	-2.1	6.6	2.9	10.8	n.a.
Excluding auto dealers	2.8	9.6	5.2	-26.6	29.1	n.a.

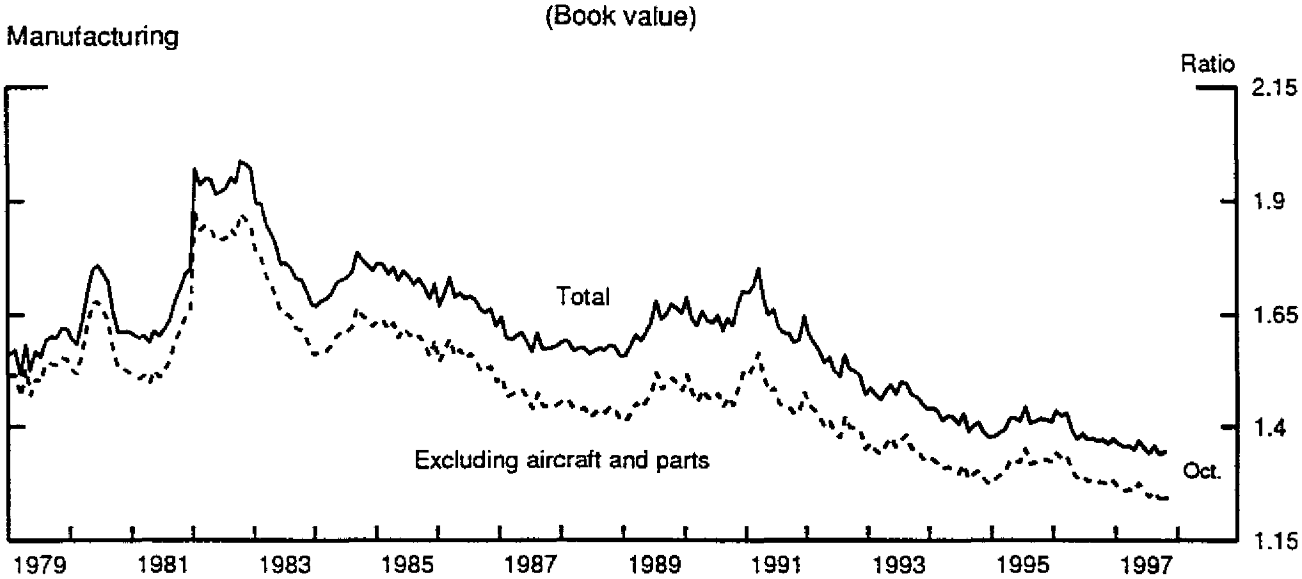
SELECTED INVENTORY-SALES RATIOS
(Months' supply, based on Census book-value data, seasonally adjusted)

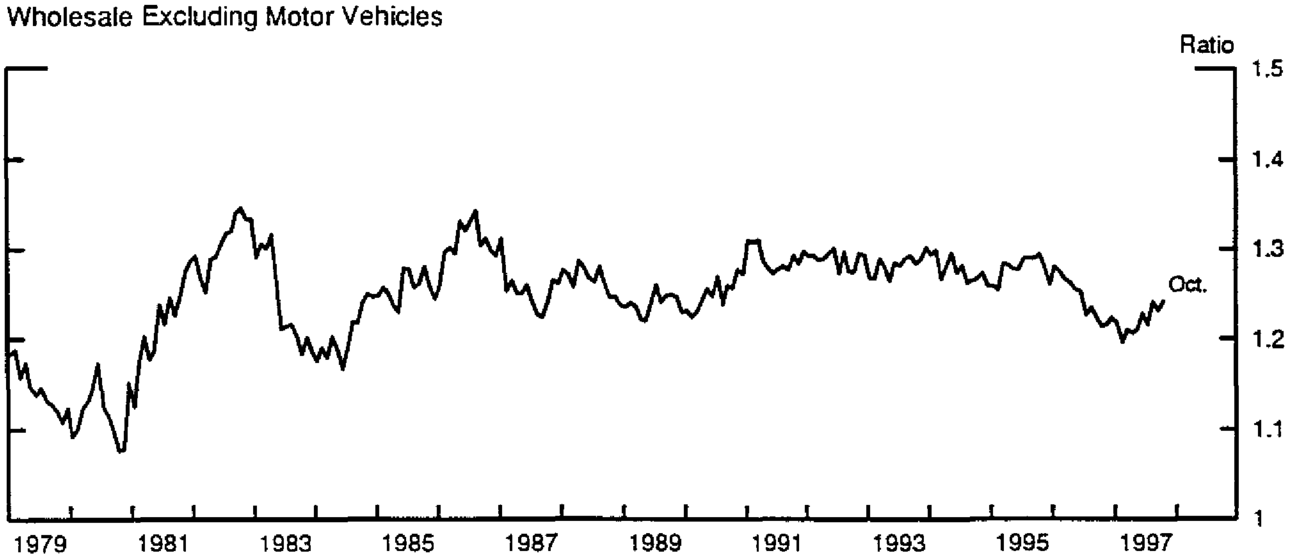
	Cyclical reference points 1990-91 high	Cyclical reference points 1995-96 low	Range over preceding 12 months High	Range over preceding 12 months Low	October 1997
Manufacturing and trade	1.58	1.37	1.38	1.35	1.36
Less wholesale and retail motor vehicles	1.55	1.34	1.35	1.32	1.33
Manufacturing	1.75	1.36	1.37	1.34	1.35
Primary metals	2.08	1.49	1.68	1.59	1.60
Nonelectrical machinery	2.48	1.80	1.87	1.71	1.72
Electrical machinery	2.08	1.41	1.46	1.29	1.32
Transportation equipment	2.93	1.48	1.61	1.52	1.56
Motor vehicles	.97	.56	.62	.56	.54
Aircraft	5.84	4.15	4.73	4.09	4.70
Nondefense capital goods	3.09	2.31	2.39	2.21	2.28
Textile	1.71	1.44	1.53	1.47	1.49
Chemicals	1.44	1.25	1.31	1.27	1.33
Petroleum	.94	.75	.84	.75	.80
Home goods & apparel	1.96	1.67	1.74	1.65	1.71
Merchant wholesalers	1.36	1.24	1.27	1.22	1.26
Less motor vehicles	1.31	1.21	1.24	1.20	1.24
Durable goods	1.83	1.53	1.56	1.50	1.53
Nondurable goods	.96	.93	.96	.92	.97
Retail trade	1.61	1.50	1.53	1.48	1.50
Less automotive dealers	1.48	1.43	1.45	1.41	1.42
Automotive dealers	2.21	1.68	1.78	1.68	1.72
General merchandise	2.43	2.21	2.26	2.08	2.10
Apparel	2.56	2.42	2.56	2.43	2.55
GAF	2.44	2.23	2.27	2.10	2.13

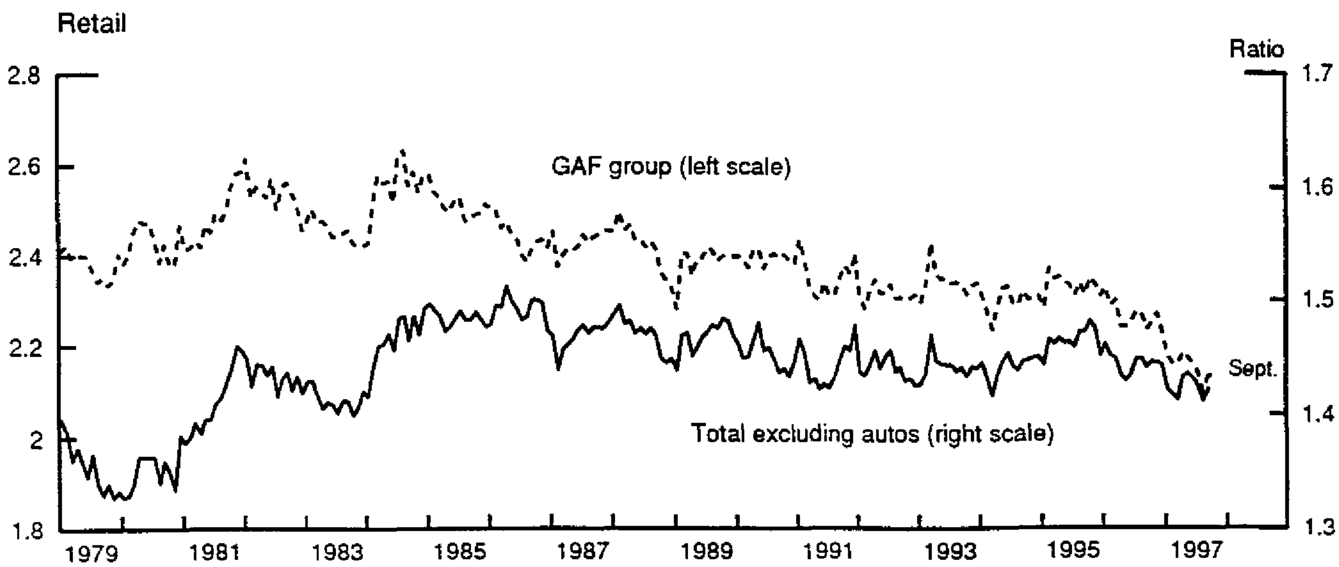
Note. October 1997 ratios for manufacturing and wholesale; September 1997 ratios for retail trade.

Inventory-Sales Ratios, by Major Sector

(Book value)







FEDERAL GOVERNMENT OUTLAYS AND RECEIPTS
(Unified basis; billions of dollars)

	October		12-month totals			
	1996	1997	Nov.95- Oct.96	Nov.96- Oct.97	Dollar change	Percent change
Outlays	139.5	150.5	1581.4	1612.3	30.9	2.0
Deposit insurance (DI)	-.1	-.4	-7.3	-14.6	-7.3	n.a.
Spectrum auction (SA)	.0	.0	-.3	-11.0	-10.7	n.a.
Other	139.6	150.9	1589.0	1638.0	48.9	3.1
Receipts	99.7	114.9	1456.7	1594.2	137.5	9.4
Deficit (+)	39.8	35.6	124.7	18.1	-106.6	-85.5
	Adjusted for payment timing shifts[1] and excluding DI and spectrum auction					
Outlays	139.6	143.3	1589.0	1630.4	41.4	2.6
National defense	22.3	24.3	269.9	272.1	2.2	.8
Net interest	21.5	21.8	242.0	244.4	2.4	1.0
Social security	29.4	30.6	351.0	366.5	15.5	4.4
Medicare	16.1	17.2	177.6	191.1	13.5	7.6
Medicaid	8.2	9.4	92.9	96.8	3.9	4.2
Other health	2.2	2.5	26.8	28.2	1.4	5.1
Income security	18.2	18.1	229.7	230.3	.6	.3
Other	21.9	19.5	199.2	201.1	1.9	1.0
Receipts	99.7	114.9	1456.7	1594.2	137.5	9.4
Individual income and payroll taxes	87.7	97.2	1134.2	1249.3	115.1	10.1
Withheld + FICA	82.8	91.6	983.9	1063.4	79.5	8.1
Nonwithheld + SECA	5.8	6.5	239.1	279.4	40.3	16.9
Refunds (-)	.9	.9	88.8	93.5	4.7	5.3
Corporate	.9	3.3	170.5	184.7	14.2	8.3
Other	11.1	14.4	152.0	160.2	8.2	5.4
Deficit(+)	39.9	28.4	132.3	36.2	-96.1	-72.7

Note. Components may not sum to totals because of rounding.

1. A shift in payment timing occurs when the first of the month falls on a weekend or holiday. The monthly and fiscal year to date outlays for defense, Medicare, income security, and "other" have been adjusted to account for this shift.

n.a. Not applicable.

In wholesale trade, stocks continued to build up at a moderate pace in October. Excluding motor vehicles, wholesale inventories increased $21 billion (annual rate) in October, about $7 billion more than the average rate for the third quarter. A surge in the accumulation of stocks of farm products ($14 billion, annual rate) accounted for much of the overall rise. This stockbuilding most likely was the result of the timing of this year's harvest, which, at the end of October, had moved ahead at an unusually rapid pace. Changes in wholesale stocks of farm products in the coming months are likely to be much smaller. With sales flat in October, the inventory-sales ratio for wholesale trade excluding motor vehicles ticked up to 1.24 months, extending its upward trend.

In retail trade, stocks of non-auto inventories increased $29 billion (annual rate) in book-value terms in September, reversing August's large decline. The inventory buildup was most notable in nondurable goods, which grew $17 billion (annual rate), the largest increase since July of last year.

Federal Government

The October Monthly Treasury Statement reported continued shrinkage in the unified deficit. Adjusted for payment timing shifts, and excluding deposit insurance and spectrum auction proceeds, the October deficit fell $12 billion from last year's level. Adjusted outlays increased only 2-1/2 percent, while receipts rose 15 percent. Withheld individual income taxes and withheld social insurance taxes (FICA), which accounted for 80 percent of total receipts in October, were up 11 percent from a year ago.

The Congress and the President have approved all thirteen regular appropriations bills funding discretionary government programs in fiscal year 1998. According to CBO, new budget authority for these programs in fiscal 1998 will increase $24 billion (5 percent) from the fiscal 1997 level. Relative to CBO's September estimates for discretionary outlays in fiscal 1997, outlays in fiscal 1998 are projected to rise only $6 billion (1 percent) because some of the increase in new budget authority--notably that for defense procurement and subsidized housing--will be spent in later years. CBO estimates that defense and nondefense discretionary outlays in fiscal 1998 will be about equal to the discretionary outlay caps legislated in the Budget Enforcement Act

CPI AND PPI INFLATION RATES
(Percent change)

	From twelve months earlier		1997		1997	
	Oct. 1996	Oct. 1997	Q2	Q3	Sept.	Oct.
			-Annual rate-		-Monthly rate-	
CPI						
All items (100.0)[1]	3.0	2.1	1.0	2.0	.2	.2
Food (15.9)	4.0	1.8	.9	3.6	.1	.2
Energy (7.0)	5.7	.9	-15.6	2.5	1.3	.1
CPI less food and energy (77.0)	2.6	2.3	2.9	1.7	.2	.2
Commodities (23.4)	1.1	.5	1.4	-1.2	.2	.1
New vehicles (5.0)	2.1	-.3	-.2	-.1	.1	-.3
Used cars (1.3)	-.1	-5.8	-7.4	-12.2	-.1	-.5
Apparel (4.8)	-1.1	.9	3.6	-2.5	.3	.1
House furnishings (3.3)	-.5	-.9	.5	-3.3	-.1	.1
Other Commodities (9.0)	2.3	2.0	2.8	1.1	.4	.3
Services (53.7)	3.2	3.0	3.5	2.8	.2	.3
Shelter (28.2)	3.1	3.1	3.4	2.8	.2	.3
Medical care (6.1)	3.2	2.7	3.3	2.2	.2	.1
Auto finance charges (0.6)	-.9	-3.7	-1.0	-2.4	-1.3	-.1
Other Services (18.8)	3.4	3.3	3.9	3.2	.1	.5
PPI						
Finished goods (100.0)[2]	3.1	-.2	-3.9	.4	.5	.1
Finished consumer foods (23.6)	5.2	-1.2	.2	-2.1	.1	.4
Finished energy (14.7)	9.8	-1.5	-22.9	5.7	1.5	.1
Finished goods less food and energy (61.6)	1.0	.3	-.5	.1	.4	.0
Consumer goods (38.1)	1.1	.6	.1	.2	.5	.1
Capital equipment (23.6)	.7	-.1	-.9	-.3	.3	-.1
Intermediate materials (100.0)[3]	.5	-.4	-2.9	-.2	.3	-.1
Intermediate materials less food and energy (81.3)	-1.6	.6	.3	.3	.0	.1
Crude materials (100.0)[4]	9.4	.3	-26.0	-3.3	.6	4.0
Crude food materials (38.0)	9.1	-8.5	7.7	-13.3	-.3	.0
Crude energy (42.4)	23.6	9.9	-58.5	7.7	2.6	10.7
Crude materials less food and energy (19.6)	-8.0	2.2	-3.7	1.2	-1.0	.3

1. Relative importance weight for CPI, December 1996.
2. Relative importance weight for PPI, December 1996.
3. Relative importance weight for intermediate materials, December 1996.
4. Relative importance weight for crude materials, December 1996.

of 1997. Meeting the spending caps in future fiscal years will be increasingly difficult because the caps increase less than $4 billion in 1999 and in 2000 and then stay about flat in 2001 and 2002.

State and Local Governments

Spending by state and local governments in the first part of the fourth quarter apparently was fairly subdued. Employment edged down 2,000 in November following an upward-revised increase of 21,000 the month before. These figures are well below the average monthly advance of 28,000 over the first nine months of the year. Real construction spending rose 0.6 percent in October, to a level slightly below the third-quarter average; much of the strength was in construction of educational facilities, while building of highways and water supply systems declined.

Prices

The incoming news on price inflation has remained favorable. The consumer price index rose 0.2 percent in October, the same rate of increase recorded in each of the past three months. Over the past twelve months, consumer prices have risen 2.1 percent, down from a 3.0 percent increase over the year-earlier period. The favorable labor cost environment, weak import prices, declining inflation expectations, and modest energy price increases have all contributed to this deceleration in the CPI.

The CPI for energy was little changed in October after having risen 3 percent over the preceding two months. Retail gasoline prices edged off in October after having risen sharply earlier partly because of a strong end-of-summer driving season. Natural gas prices rose 2.4 percent in October after a similar increase in September as demand was pushed up by higher prices for some substitute fuels and rail supply disruptions forced some electric utilities to substitute gas for coal. Over the past twelve months, energy prices have risen only 0.9 percent, down considerably from the 5-3/4 percent increase in the year-earlier period.

Retail food prices rose 0.2 percent in October, close to their average rate of increase over the past few months. The CPI for food away from home was up just 0.1 percent in October; although wages at eating and drinking establishments jumped in September with the rise in the minimum wage, the pass-through of higher wage costs into food prices has thus far been only modest. Overall, the CPI for food was up 1.8 percent over the twelve months ended in October, more than

BROAD MEASURES OF INFLATION
(Four-quarter percent change)

	1994 Q3	1995 Q3	1996 Q3	1997 Q3
Product prices				
GDP chain price index	2.5	2.5	2.4	1.9
Nonfarm business chain-type price index[1]	2.6	2.1	1.7	1.6
Expenditure prices				
Gross domestic purchases chain-type price index	2.5	2.4	2.2	1.6
Less food and energy	2.5	2.6	2.0	1.6
PCE chain-type price index	2.7	2.4	2.4	1.9
Less food and energy	2.8	2.7	2.1	1.9
CPI	2.9	2.6	3.0	2.2
Less food and energy	2.9	3.0	2.7	2.3
Median CPI	2.9	3.1	3.0	2.8

1. Excluding housing

SURVEYS OF (CPI) INFLATION EXPECTATIONS
(Percent)

	Actual inflation[1]	University of Michigan (1-year) Mean[2]	University of Michigan (1-year) Median[3]	Conference Board (1-year)	Professional forecasters (10-year)[4]
1996-Q1	2.7	3.9	2.9	4.1	3.0
Q2	2.8	4.5	3.0	4.3	3.0
Q3	2.9	4.2	3.0	4.3	3.0
Q4	3.2	4.0	3.0	4.2	3.0
1997-Q1	2.9	3.8	2.9	4.2	3.0
Q2	2.3	3.6	2.9	4.0	2.9
Q3	2.2	3.4	2.7	4.0	3.0
Q4					2.7
Jul	2.2	3.4	2.7	4.0	
Aug.	2.2	3.3	2.7	3.9	
Sept.	2.2	3.5	2.8	4.1	3.0
Oct.	2.1	3.2	2.8	4.1	
Nov.		3.4	2.9	4.1	
Dec.					2.7

1. CPI; percent change from the same period in the preceding year.
2. Average increase for responses to the question: By about what percent do you expect prices (CPI) to go up, on the average, during the next 12 months?
3. Median increase for responses to the question above.
4. Compiled by the Federal Reserve Bank of Philadelphia.

2 percentage points less than the increase over the preceding twelve months. Although recent data on farm commodity prices suggest that retail food prices could blip up in the very near term, the increases appear likely to be concentrated in categories--such as eggs and fresh vegetables--in which price spurts typically are short-lived.

For items other than food and energy, consumer prices rose 0.2 percent in October, continuing a string of small increases. On a twelve-month-change basis, the core CPI was up 2.3 percent in October, down 1/4 percentage point from the pace registered a year earlier.[5] Prices of both goods and services other than food and energy registered some deceleration over the past year. Among goods, falling import prices have been an important restraining influence on prices in recent years. This restraint has been most clearly evident in the prices of new motor vehicles, which declined slightly over the twelve months ended in October after having risen more than 2 percent over the preceding year. (The deceleration in new and used auto prices accounts for most of the 1/4 percentage point deceleration in the core CPI over the last year.) The pace of price increases of many other goods also was lower over the past year; apparel was one notable exception, having picked up about 2 percentage points. Among services other than energy, price increases slowed for many items, including medical care and auto finance charges.

Broad expenditure price measures other than the CPI also slowed over the past year. Core PCE prices continued to decelerate over the past year, about in line with the core CPI over the past two years. Among product prices, the pace of increase in the GDP chain price measure has moved down about 1/2 percentage point over the past four quarters.

Inflation expectations as measured by the Michigan SRC index have also come down over the past year, although they ticked back up a bit in November. In the third quarter of this year, one-year-ahead median expectations were about 1/4 percentage point lower than a year earlier, while mean expectations were about 3/4 percentage point lower. And ten-year-ahead mean inflation expectations of professional forecasters surveyed by the Federal Reserve Bank of Philadelphia were down 0.3 percentage point from a year ago.

5. The deceleration is about the same magnitude after adjusting for technical changes in the CPI.

SPOT PRICES OF SELECTED COMMODITIES

	Current price ($)	Percent change[1]: 1995	1996	Dec. 31 to Nov. 04[2]	Nov. 04[2] to Dec. 09	Memo: Year earlier to date
Metals						
Copper (lb.)	.850	-3.5	-18.3	-11.2	-10.5	-21.3
Steel scrap (ton)	131.500	-6.6	-13.7	19.7	-5.7	12.9
Aluminum, London (lb.)	.704	-12.9	-9.8	4.8	-2.0	5.0
Precious metals						
Gold (oz.)	283.250	1.7	-5.1	-14.6	-10.2	-23.1
Silver (oz.)	5.360	7.2	-8.8	1.9	10.2	12.0
Forest products						
Lumber (m. bdft.)	292.000	-14.4	66.0	-25.8	-5.2	-29.6
Plywood (m. sqft.)	295.000	-6.1	1.6	-2.9	-3.6	-6.3
Petroleum						
Crude oil (barrel)	17.460	16.8	25.9	-18.8	-9.1	-26.8
Gasoline (gal.)	.521	7.7	24.3	-17.8	-6.1	-21.9
Fuel oil (gal.)	.524	22.6	16.1	-19.1	-8.0	-25.1
Livestock						
Steers (cwt.)	68.000	-5.7	.0	3.0	.0	3.0
Hogs (cwt.)	44.500	27.5	34.1	-18.2	-1.1	-20.5
Broilers (lb.)	.487	10.7	12.4	-19.4	-3.5	-21.7
U.S. farm crops						
Corn (bu.)	2.670	57.4	-29.5	6.3	-1.5	2.3
Wheat (bu.)	3.925	24.0	-16.6	-15.3	1.9	-18.1
Soybeans (bu.)	6.990	29.0	-7.1	2.3	-.7	2.9
Cotton (lb.)	.644	-8.1	-10.9	-1.0	-8.1	-11.2
Other foodstuffs						
Coffee (lb.)	1.910	-39.1	43.2	8.5	29.5	50.4
Memo:						
JOC Industrials	100.400	-1.7	-3.7	-1.9	-4.7	-5.9
JOC Metals	90.800	-1.8	-7.7	1.1	-3.9	-1.8
KR-CRB Futures	237.110	3.3	-2.6	1.4	-1.9	-1.6
KR-CRB Spot	310.290	-3.5	1.0	-.9	-6.5	-6.5

1. Changes, if not specified, are from the last week of the preceding year to the last week of the period indicated.
2. Week of the November Greenbook.

The PPI for capital equipment edged down in October and stood about unchanged from its year-earlier level, compared with an increase of 0.7 percent over the previous twelve months. In October, the capital goods index was held down by a drop in truck prices. However, computer prices reportedly were unchanged in October after having fallen on average nearly 2 percent per month so far this year.[6]

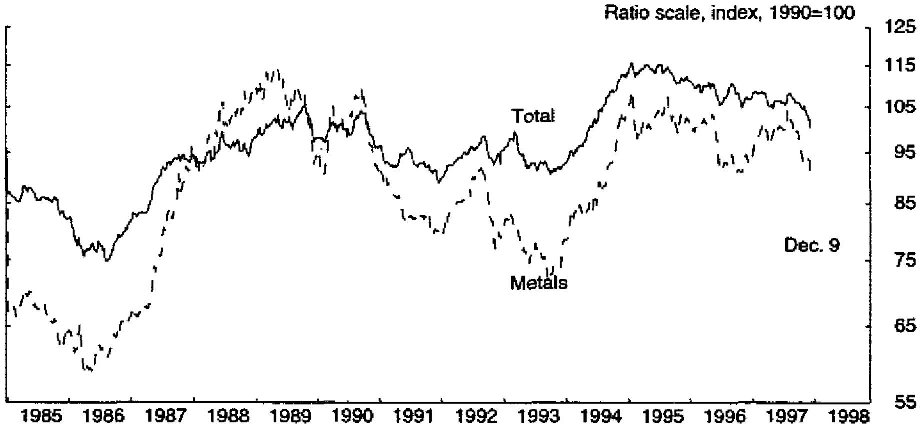
Prices at earlier stages of processing have also been restrained lately. The PPI for core intermediate materials only edged up in October, and the index for core crude materials rebounded only partially from a decline in September.

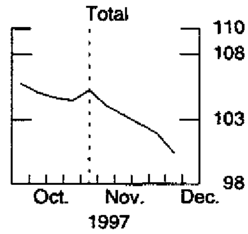
In addition, price indexes for industrial commodities have plummeted since the time of the last Greenbook. The Journal of Commerce industrial price index, in which price changes are "standardized" to take account of historical volatility, has dropped about 5 percent since early November, and the CRB price index for spot industrials has fallen about 6-1/2 percent. Declines over this period have been widespread among metals, textiles, and other industrial inputs such as hides and rubber. Prices of food commodities--and the indexes in which these commodities are given large weight--also are down on balance since early November, but by a much smaller amount than the industrial price measures.

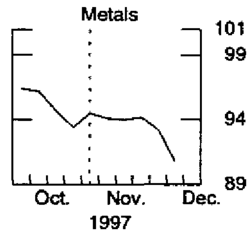
6. The October reading reflected big price increases for larger computers: prices of personal computers fell at close to their average rate so far this year.

Commodity Price Measures

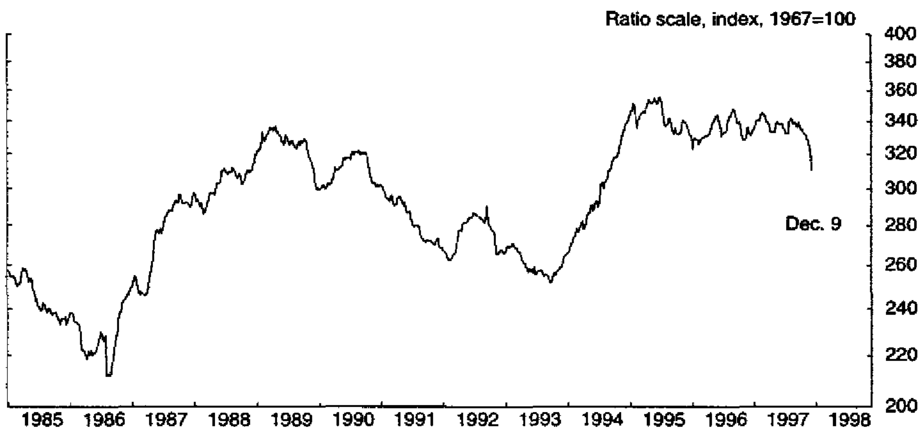
Journal of Commerce Index

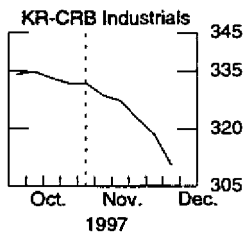




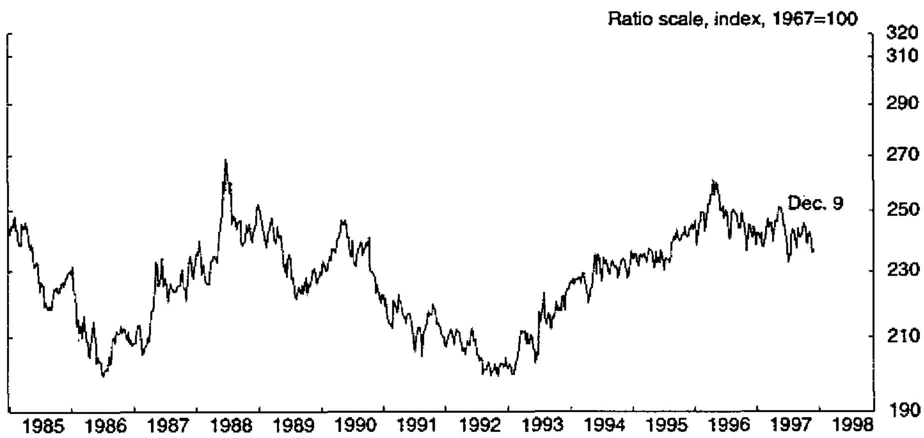


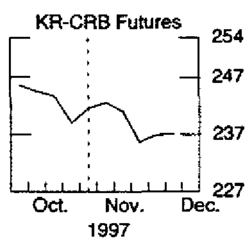
KR-CRB Spot Industrials





KR-CRB Futures





Note. Weekly data, Tuesdays. Vertical lines on small panels indicate week of last Greenbook. The Journal of Commerce index is based almost entirely on industrial commodities, with a small weight given to energy commodities, and the KR-CRB spot price index consists entirely of industrial commodities, excluding energy. The KR-CRB futures index gives about a 60 percent weight to food commodities and splits the remaining weight roughly equally among energy commodities, industrial commodities, and precious metals. Copyright for Journal of Commerce data is held by CIBCR, 1994.

DOMESTIC FINANCIAL DEVELOPMENTS

Selected Financial Market Quotations[1]
(Percent except as noted)

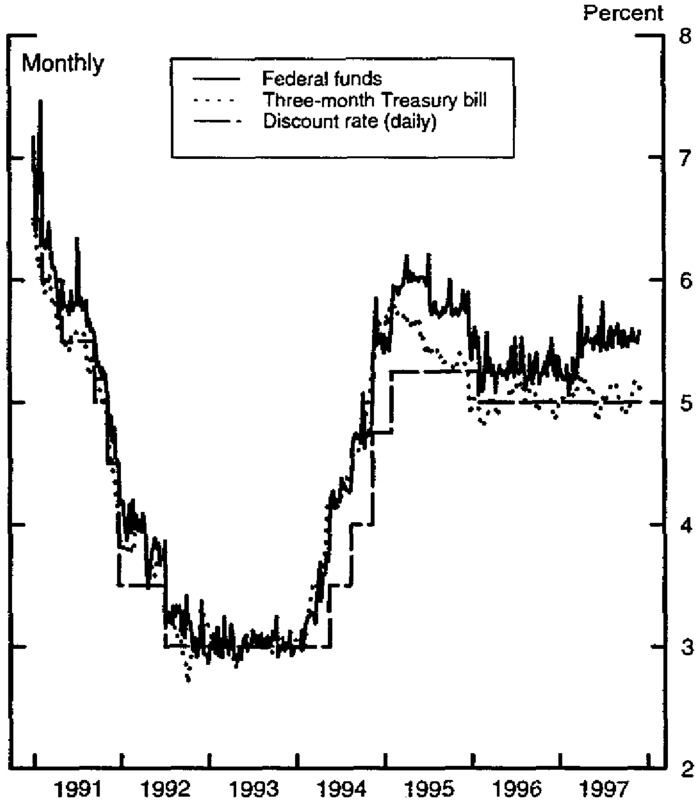
Instrument	1997 Jan. 2	1997 Mar. low	1997 FOMC * Nov. 12	1997 Dec. 10	Change to Dec.10, from: Jan. 2	Change to Dec.10, from: Mar. low	Change to Dec.10, from: FOMC * Nov. 12
Short-term rates							
Federal funds [2]	5.79	5.27	5.50	5.40	-.39	.13	-.10
Treasury bills [3]							
3-month	5.05	5.04	5.21	5.07	.02	.03	-.14
6-month	5.14	5.17	5.17	5.22	.08	.05	.05
1-year	5.28	5.37	5.17	5.22	-.06	-.15	.05
Commercial paper [4]							
1-month	5.48	5.40	5.53	5.75	.27	.35	.22
3-month	5.47	5.45	5.54	5.69	.22	.24	.15
Large negotiable CDs [3]							
1-month	5.39	5.32	5.57	5.88	.49	.56	.31
3-month	5.42	5.42	5.70	5.81	.39	.39	.11
6-month	5.50	5.58	5.75	5.86	.36	.28	.11
Eurodollar deposits [5]							
1-month	5.38	5.31	5.50	5.88	.50	.57	.38
3-month	5.44	5.44	5.63	5.81	.37	.37	.18
Bank prime rate	8.25	8.25	8.50	8.50	.25	.25	.00
Intermediate- and long-term rates							
U.S. Treasury (constant maturity)							
3-year	6.13	6.25	5.78	5.79	-.34	-.46	.01
10-year	6.54	6.56	5.91	5.90	-.64	-.66	-.01
30-year	6.75	6.83	6.15	6.10	-.65	-.73	-.05
U.S. Treasury 10-year indexed note	n.a.	3.36	3.55	3.58	n.a.	.22	.03
Municipal revenue (Bond Buyer) [6]	5.96	5.97	5.65	5.48	-.48	-.49	-.17
Corporate-A utility, recently offered	7.64	7.97	7.30	7.22	-.42	-.75	-.08
High-yield corporate [7]	9.72	9.49	9.06	9.07	-.65	-.42	.01
Home mortgages [8]							
FHLMC 30-yr fixed rate	7.64	7.84	7.24	7.15	-.49	-.69	-.09
FHLMC 1-yr adjustable rate	5.57	5.54	5.53	5.50	-.07	-.04	-.03

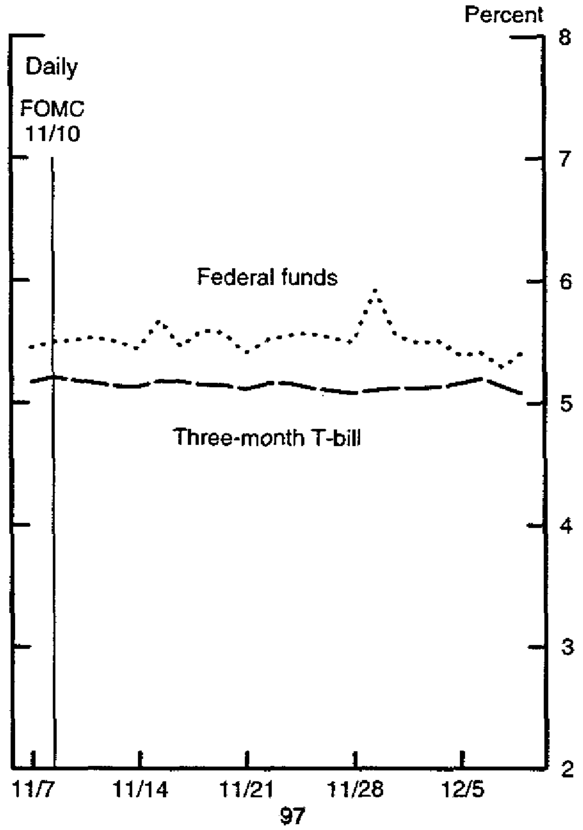
Stock exchange index	Record high Level	Record high Date	1997 Jan. 2	1997 FOMC * Nov. 12	1997 Dec. 10	Percentage change to Dec. 10, from: Record high	Percentage change to Dec. 10, from: Jan. 2	Percentage change to Dec. 10, from: FOMC * Nov. 12
Dow-Jones Industrial	8259.31	8/6/97	6441.49	7552.59	7978.79	-3.40	23.87	5.64
S&P 500 Composite	983.79	12/5/97	736.01	921.13	969.79	-1.42	31.76	5.28
NASDAQ (OTC)	1745.85	10/9/97	1279.70	1590.72	1596.61	-8.55	24.76	.37
Russell 2000	465.21	10/13/97	357.96	435.40	432.81	-6.96	20.91	-.59
Wilshire	9486.69	10/7/97	7146.80	8917.32	9272.23	-2.26	29.74	3.98

1. One-day quotes except as noted.
2. Average for two-week reserve maintenance period closest to date shown. Last observation is the average to date for maintenance period ending December 17,1997.
3. Secondary market.
4. As of September 2, 1997, commercial paper rates are those collected by the Depository Trust Company; prior rates are averages of offering rates at several large dealers.
5. Bid rates for Eurodollar deposits at 11 a.m. London time.
6. Most recent observation based on one-day Thursday quote and futures market index changes.
7. Merrill Lynch Master II high-yield bond index composite.
8. Quotes for week ending Friday previous to date shown.
* Figures cited are as of the close on November 10, 1997.

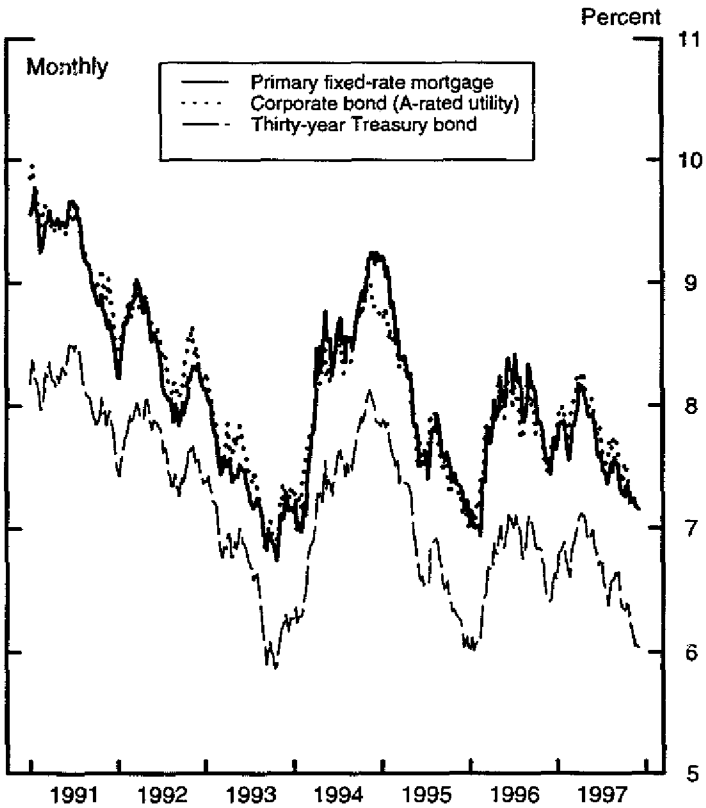
Selected Interest Rates

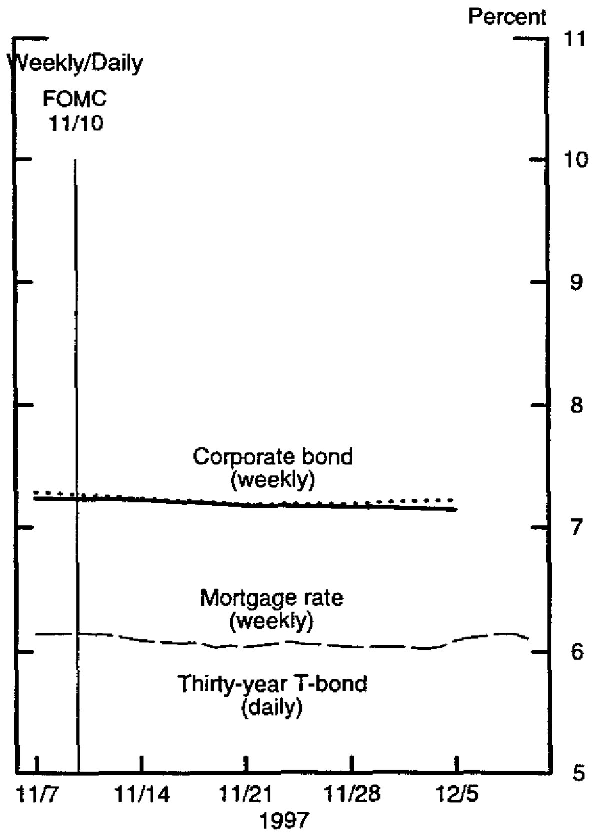
Short-Term





Long-Term





DOMESTIC FINANCIAL DEVELOPMENTS

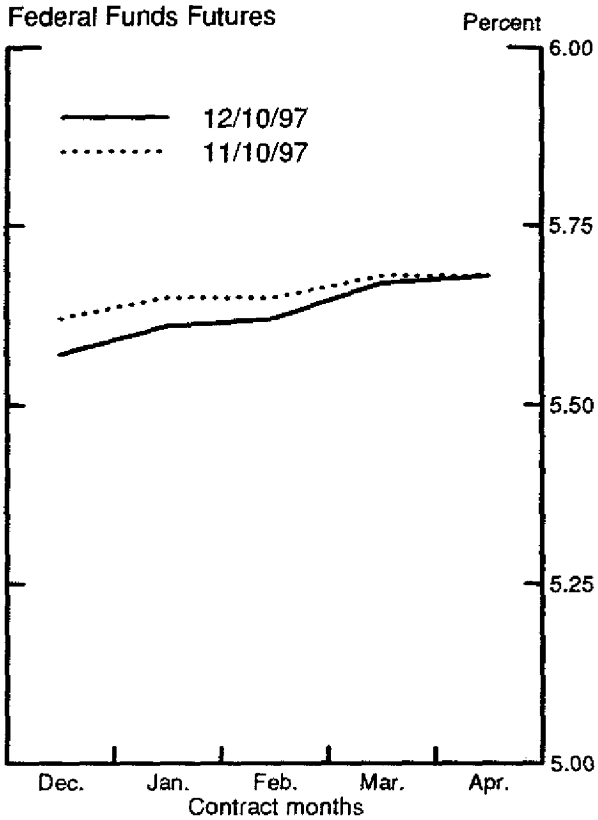
The decision by the FOMC to keep the federal funds rate at 5-1/2 percent at its November meeting was widely expected and elicited little market response. In the weeks that followed, spreading strains in Asia solidified the sentiment that additional policy restraint would not be needed to contain inflation, and, with economic data suggesting that domestic considerations would not otherwise force policymakers' hands, most interest rates moved lower. In recent days, though, surprising strength in the November employment report raised the question as to whether System action might not be needed at some point, causing market interest rates to roll back some of their earlier declines. On net, over the intermeeting period, most interest rates have shown rather narrow, mixed changes, and spreads of private over Treasury rates have held steady. The exception to that pattern is one-month rates, which bumped much higher when that maturity crossed the year-end. Futures rates currently price in about 1 to 2 percentage points of year-end pressures in the federal funds market; these pressures about match the average expectations before year-end of the past five years (chart).

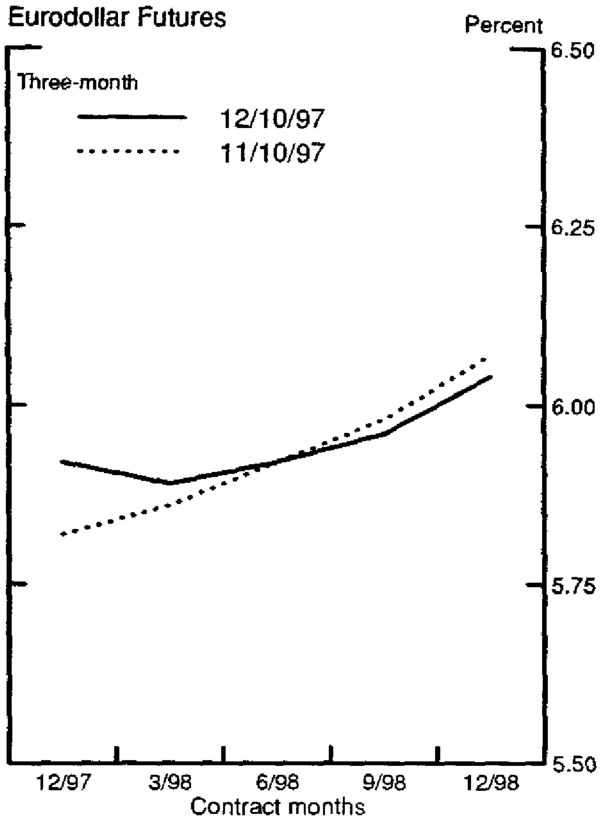
Major equity indexes have gained 4 percent to 6 percent over the intermeeting period, reversing much of the price declines of late October. The notable exception has been the NASDAQ composite, which has been held down by the recent poor performance of technology stocks. Over the year to date, equity indexes have risen about 20 percent to 30 percent. The modest outflow from equity mutual funds in late October proved transitory; households have resumed fairly healthy net purchases of such funds. The main exception has been international funds, which have become less attractive to investors.

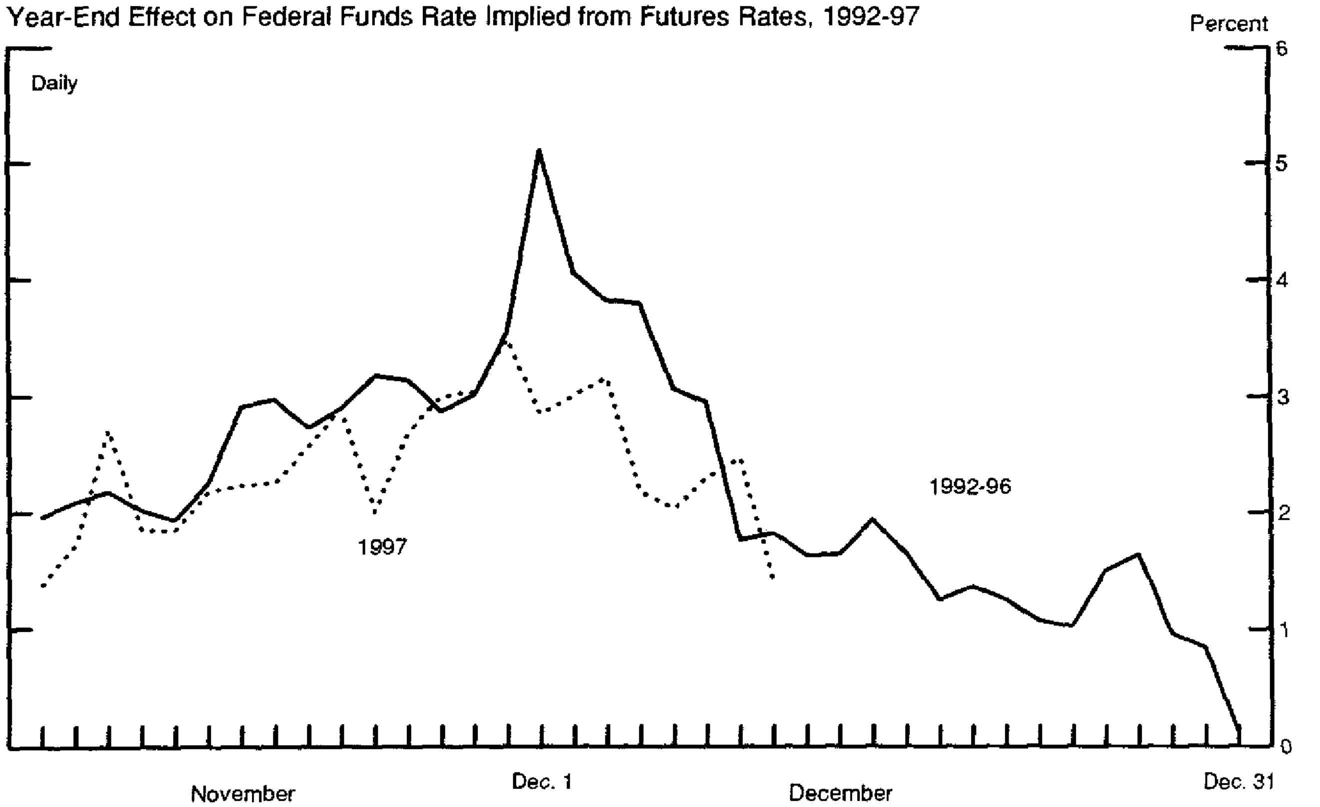
Indicators of market skittishness have receded from the spikes of late October. Volatility inferred from option prices on both bonds and equities has dropped to levels prevailing before the market correction. Although risk spreads on fixed-income instruments have retraced only part of their late-October runup, the spreads remain on the narrow side, judging by historical ranges.

With markets remaining quite receptive, bond issuance by nonfinancial businesses has picked up recently after slowing in November; equity issuance by nonfinancial companies has remained

Financial Market Futures and Their Year-End Effects on the Federal Funds Rate







fairly robust, although the price performance of new stock offerings has been considerably less exuberant than it was earlier this year. Borrowing by households appears to have strengthened in October, and recent indicators of household credit quality point to a leveling out of debt strains in this sector. Treasury borrowing has remained light, forcing further cuts in auction sizes. Growth of the broader monetary aggregates turned up in November, boosted by currency demands and a turnaround in liquid deposits.

Business Finance

Despite the decline in bond yields in November, gross corporate bond issuance fell off sharply last month (table and chart). The investment-grade sector, which in recent quarters has been issuing debt primarily to fund mergers and acquisitions, accounts for the bulk of the decline. For firms of investment-grade status, mergers and takeovers involving cash payments are typically funded first with commercial paper, which is rolled over until later replaced by a bond offering. In November, a number of large mergers were financed with commercial paper, but the rumored bond issues were either postponed or trimmed in size.

Speculative-grade bond issuance stayed at a fairly high level in November and early December. Although interest rate spreads increased from their record-low levels of October, they remain subdued by historical standards. In addition, corporate credit quality appears to be solid. Business failures in October and November dropped significantly from already low rates posted earlier in the year, and the default rate on junk bonds has remained very low.

Recent swings in stock prices left little imprint on public equity issuance, as offerings by nonfinancial companies remained high in November (table and chart). The volume of IPOs hit $3.3 billion in November, the largest monthly volume this year. However, the price performance of these deals deteriorated noticeably. Most of the issues were completed with offering prices below the filing price range, and first-day price increases for IPOs averaged a mere 6-1/2 percent, down from 22 percent in October. In addition, more than 80 percent of seasoned offerings in November fell in price. Meanwhile, equity retirements have remained very heavy. Companies continue to announce stock repurchase plans at a near-record pace, and ongoing merger activity will result in about $25 billion of equity retirements in the fourth quarter.

GROSS ISSUANCE OF SECURITIES BY U.S. CORPORATIONS
(Billions of dollars; monthly rates, not seasonally adjusted)

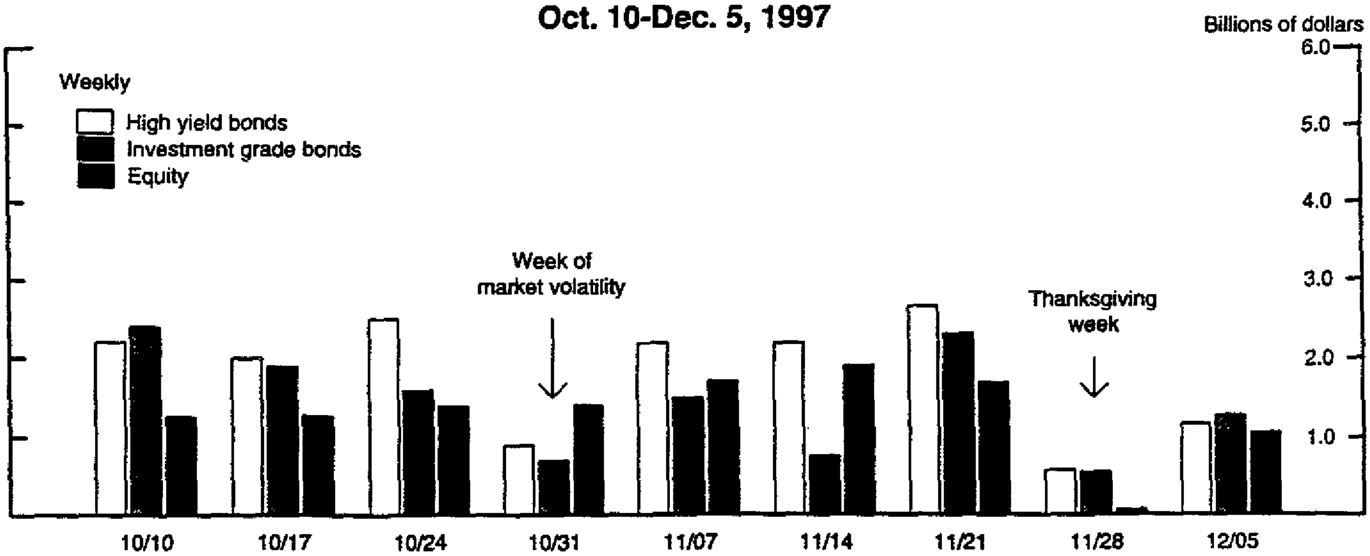
Type of security	1995	1996	1997 Q2	1997 Q3	1997 Sept.	1997 Oct.	1997 Nov.
All U.S. corporations	47.6	58.4	68.8	74.9	89.3	67.6	58.3
Stocks[1]	6.1	10.2	9.1	8.7	10.4	12.8	11.0
Bonds	41.5	48.2	59.7	66.2	78.9	54.7	47.3
Nonfinancial corporations							
Stocks[1]	4.4	6.7	4.4	5.2	6.4	6.6	6.3
Initial public offerings	1.7	2.9	1.9	1.8	2.1	2.8	3.3
Seasoned offerings	2.7	3.8	2.5	3.4	4.3	3.8	3.1
Bonds	10.7	12.5	17.4	22.1	20.7	20.2	12.8
By rating, sold in U.S.[2]							
Investment grade	6.4	6.3	7.1	9.9	8.0	9.5	5.4
Speculative grade	3.0	4.8	8.7	9.1	9.0	9.2	6.9
Public	2.0	2.3	1.4	1.0	1.1	.7	.5
Rule 144A	1.1	2.5	7.4	8.1	7.9	8.5	6.4
Financia corporations							
Stocks[1]	1.7	3.5	4.7	3.5	4.0	6.2	4.7
Bonds	30.8	35.8	42.3	44.1	58.2	34.6	34.5
MEMO:							
Net issuance of nonfinancial commercial paper (end-of-period basis)	1.6	-.1	1.8	.8	-0.3	2.5	5.8
Change in C&I loans at commercial banks (end-of-period basis)	6.0	5.6	5.0	7.8	10.5	2.7	13.2

Note. Components may not sum to totals because of rounding. These data include speculative-grade bonds issued privately under Rule 144A. All other private placements are excluded. Total reflects gross proceeds rather than par value of original discount bonds.

1. Excludes equity issues associated with equity-for-equity swaps that have occurred in restructurings.

2. Bonds categorized according to Moody's bond ratings, or to Standard & Poor's if unrated by Moody's. Excludes mortgage-backed and asset-backed bonds.

Gross Offerings of Nonfinancial Corporate Securities
Oct. 10-Dec. 5, 1997



Equity prices rebounded over the intermeeting period, and the NYSE and S&P 500 indexes topped their peak October levels before dropping back in recent days. Earnings disappointments and downward revisions to projected earnings picked up some of late, but mostly they have been concentrated in the technology sector in which exposures to Asian problems also have raised concerns. Reflecting the heavy weighting of technology stocks, the NASDAQ index remains about 8-1/2 percent below its October peak (chart, upper panel). Overall expectations of earnings growth, however, remain surprisingly upbeat. The consensus of Wall Street strategists' 1998 profit projections implies 7 percent growth in S&P 500 earnings next year, little different from the view of two months ago. In addition, longer-term (five-year) growth projections for the S&P 500, constructed from I/B/E/S surveys of company analysts, remain at the record-high levels of September (chart, middle left panel).

To be sure, this optimism is fueled by continued exceptional corporate performance. As with earnings per share for the S&P 500, growth in NIPA book profits rebounded in the third quarter (chart, middle right panel). On a seasonally adjusted basis, third-quarter NIPA profits were up roughly 2-3/4 percent from the second quarter and 10-1/2 percent from a year earlier. However, price-earnings ratios are at all-time highs (chart, lower panel) and, given the late stage of the current expansion, suggest extraordinary optimism about corporate prospects.

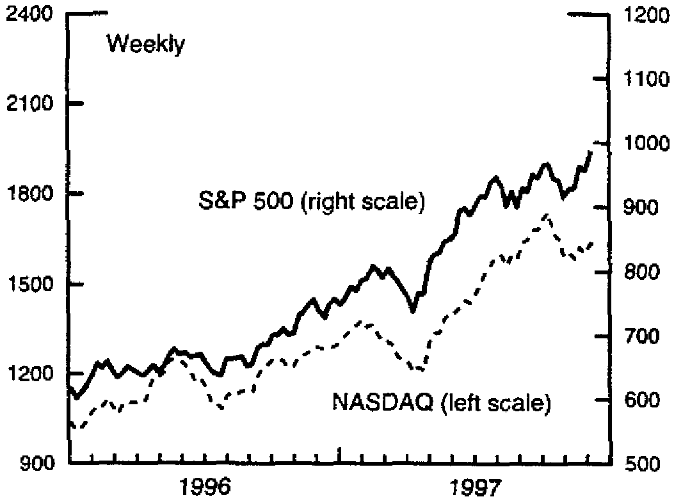
Mutual Funds

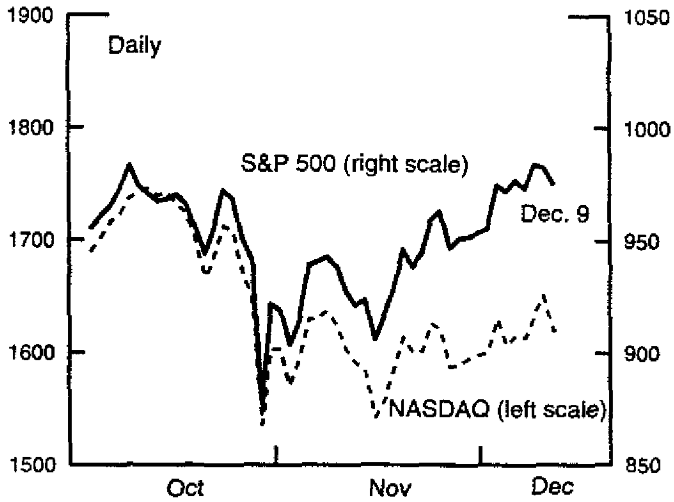
Mutual fund investors' enthusiasm for equities cooled off somewhat after the market correction of late October. Equity funds posted a net outflow in the last week of that month. According to preliminary estimates, inflows recovered in November but at only half the pace of the prior two months (table). Concerns about Asian and Latin American markets generated a rare monthly net outflow from international funds. Net inflows to domestic growth funds dropped from the high levels posted in the third quarter. To some extent, the stock market's gyrations heightened investors' interest in bond funds, which are more stable. As a result of this substitution, the net inflow to bond funds picked up well above its third-quarter pace.

Liquidity ratios at equity funds remain around 5 percent, a low level by historical standards although they proved adequate to meet limited investor withdrawals when they have occurred in recent weeks

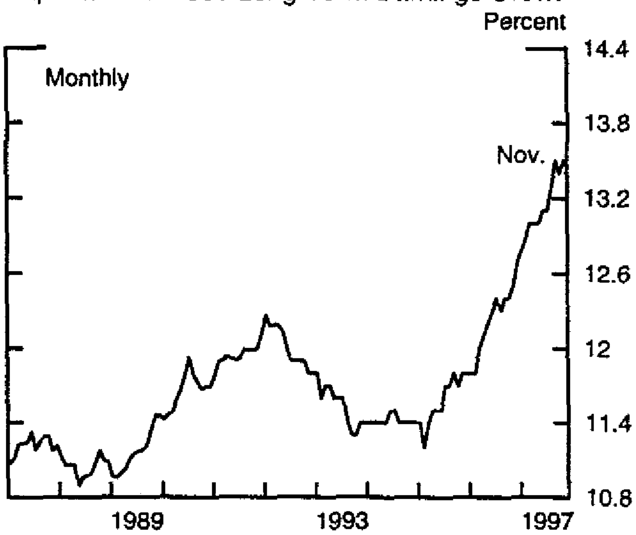
Corporate Finance

Equity Prices



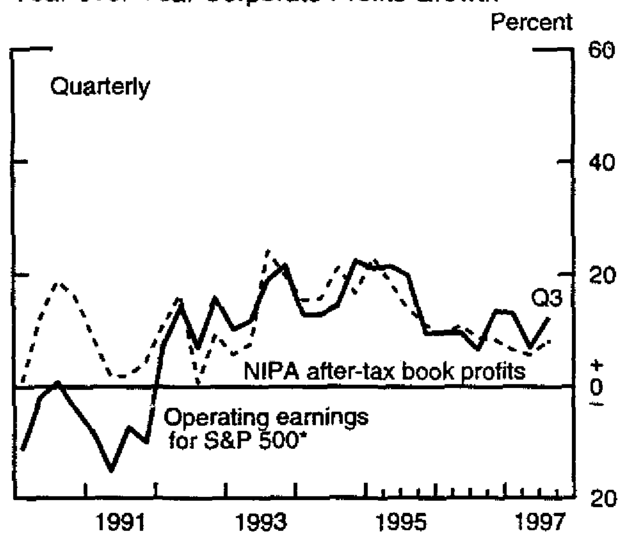


Expected S&P 500 Long-Term Earnings Growth



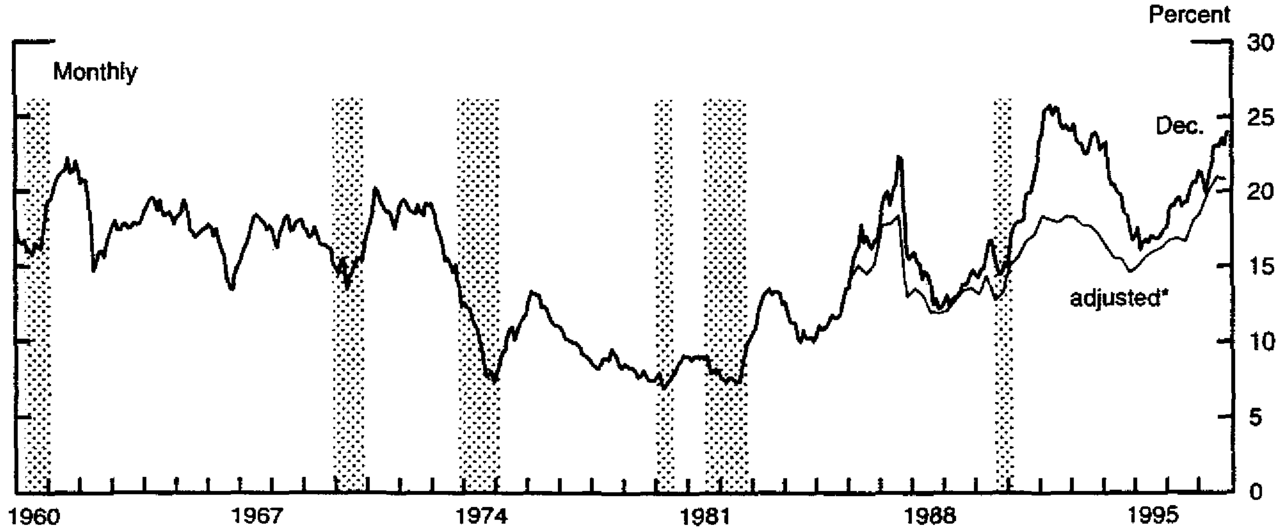
Source. I/B/E/S.

Year-over-Year Corporate Profits Growth



*Source. Goldman Sachs.

S&P 500 Price-Earnings Ratio



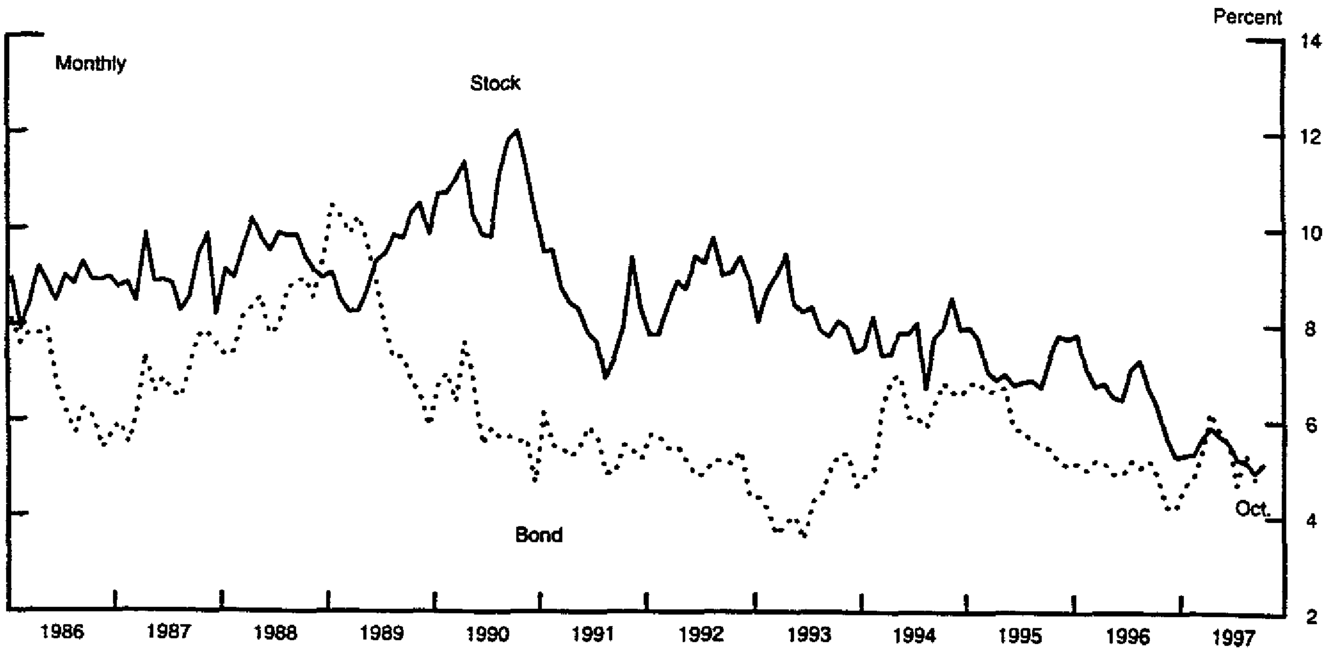
*Based on Goldman Sach's estimates of S&P 500 quarterly operating earnings.

Net Sales of Selected Mutual Funds
(Excluding Reinvested Distributions)
(Billions of dollars; quarterly and annual data at monthly rate)

	1995	1996	1997 Q2	1997 Q3	1997 Sep.	1997 Oct.	1997 Nov.[e]	1997 Oct. Assets
Stock Funds	**10.7**	**18.5**	**18.7**	**22.2**	**25.8**	**18.2**	**11.6**	**2,301**
Domestic equity[1]	9.7	14.7	13.9	18.7	22.2	18.2	13.0	1,953
Aggressive Growth	3.1	4.7	2.4	4.8	7.8	4.0	2.5	360
Growth	3.1	3.9	3.2	5.9	7.1	5.8	2.9	640
Growth and Income	3.7	6.2	8.3	7.9	7.0	8.6	7.8	949
International	1.0	3.9	4.8	3.5	3.6	0.0	-1.4	348
Bond funds	**-0.4**	**1.2**	**3.0**	**5.1**	**3.9**	**3.7**	**7.2**	**996**
High-yield	0.7	1.0	1.7	1.6	1.8	0.9	1.8	99
Balanced	0.5	0.9	1.8	1.8	1.8	1.2	2.1	301
Other	-1.6	-0.7	-0.5	1.7	0.3	1.6	3.4	596

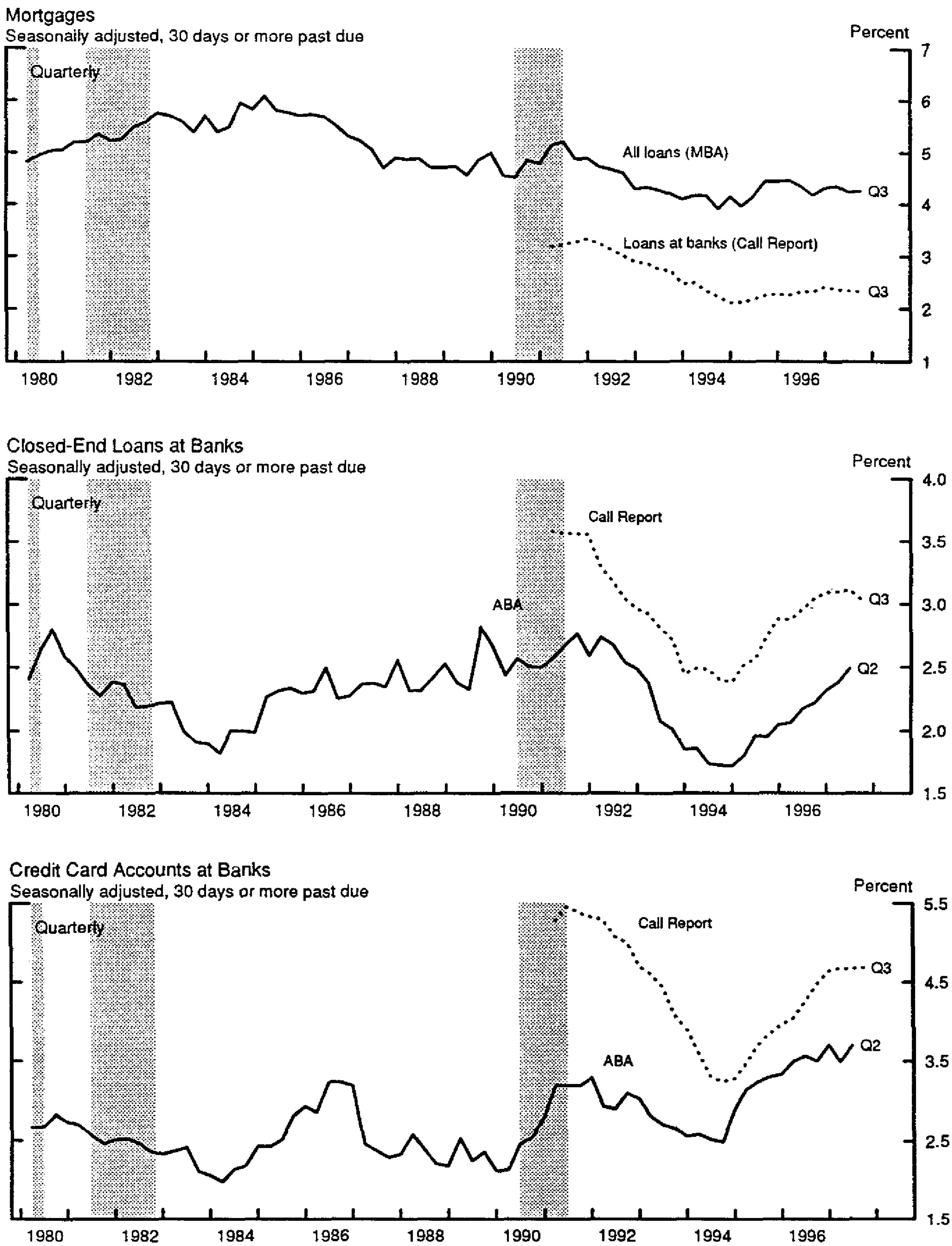
Source: Investment Company Institute (ICI)
1. Includes precious metals funds not shown elsewhere.
e Staff estimates, based on weekly ICI totals.

Liquidity Ratios for Domestic Long-Term Mutual Funds



Note. Liquidity ratio is cash and short-term securities as a percent of total assets.
Source. Investment Company Institute.

Delinquency Rates on Household Loans



Note. The MBA and ABA series are by number of loans; the Call Report series are by dollar volume.

(chart). Many mutual funds reportedly have secured committed lines of credit from banks and other backup sources to supplement liquidity in the event of heavy withdrawals.

Banking

The share prices of money center banks were hard-hit by the financial market turmoil of late October and November but have since about caught up with the S&P 500. Evidently, market participants came to the realization that, in the aggregate, banks' exposure to Asia was not sizable enough to affect the health of the industry significantly. Country exposure reports through June indicate that money center banks had about $38 billion of loans to Japan and $27 billion to other troubled countries in Asia; for the banking system as a whole, that aggregate exposure represents a small proportion of banks' capital. Nonetheless, a number of money center banks have reported negative effects on fourth-quarter earnings as a result of unsettled conditions in global markets.

Data from the September Call Report indicate that loan delinquency rates at banks held steady or even improved a bit (chart). However, in the most recent survey of senior Federal Reserve bank examiners, a third of the respondents indicated that they believed that loan portfolio quality had deteriorated in the third quarter, owing to problems with credit card loans. About a quarter of the examiners had reported some deterioration in the second quarter.

Household Sector

Consumer credit grew 10-1/2 percent at an annual rate in October, as all three major components accelerated from the prior month (table). Smoothing through monthly swings, consumer debt seems to be expanding at about the same rate as personal income. Data on mortgage borrowing in the fourth quarter are scarce: Growth in real estate loans at commercial banks slowed in October to about half the third-quarter pace but appears to have picked up in November. Meanwhile, the MBA indexes of applications for purchase and refinance remain quite high, suggesting healthy mortgage borrowing.

Following the recent flattening of the yield curve, the spread between the initial rate on fixed-rate mortgages (FRMs) and that on adjustable-rate mortgages (ARMs) has fallen to a near-record low level of 165 basis points (chart). The relative attractiveness of FRMs has been reflected in a declining share of ARM originations, to

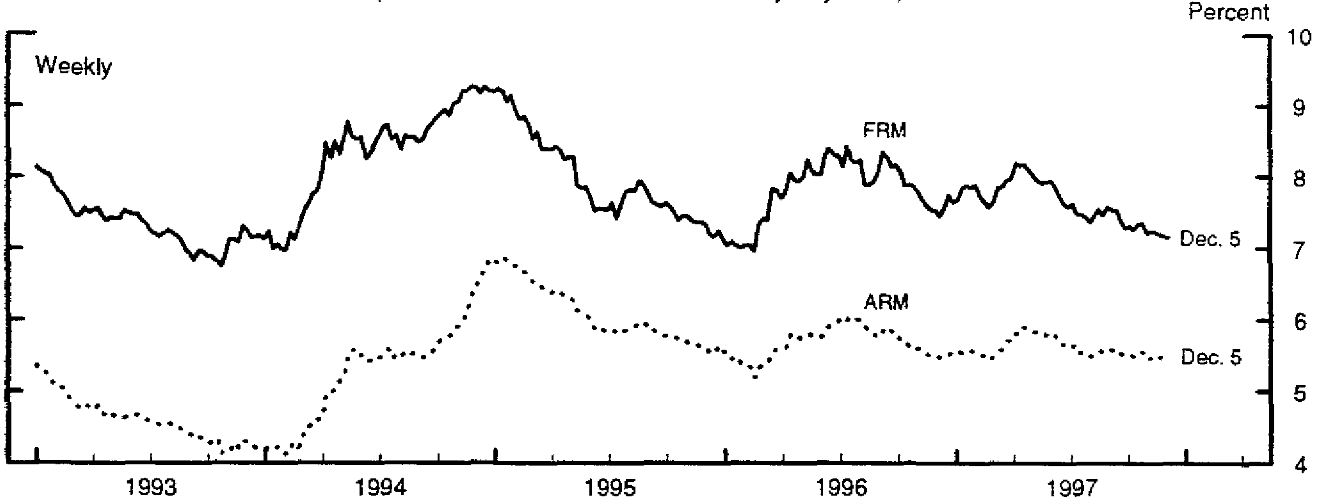
Consumer Credit

	1995	1996	1997 Q1	1997 Q2	1997 Q3	1997 Aug	1997 Sep	1997 Oct[p]
Credit outstanding, end of period								
Growth rates (percent, SAAR)								
Total	14.0	7.8	5.9	4.8	3.5	6.1	0.6	10.5
(Previous)	*(14.1)*	*(7.6)*	*(7.0)*	*(2.8)*	*(4.0)*	*(4.2)*	*(1.9)*	
Auto	11.1	7.7	0.3	7.3	3.9	-2.2	5.6	12.5
Revolving	21.2	12.7	8.2	5.3	7.7	7.9	5.8	8.1
Other	7.7	0.5	9.5	0.8	-4.4	14.0	-15.2	12.0
Levels (billions of dollars, SA)								
Total	1094.2	1179.9	1197.3	1211.7	1222.4	1221.7	1222.4	1233.1
Auto	364.2	392.4	392.6	399.8	403.7	401.9	403.7	407.9
Revolving	443.0	499.2	509.5	516.2	526.2	523.6	526.2	529.7
Other	287.0	288.3	295.2	295.8	292.5	296.3	292.5	295.5
Interest rates[1] (annual percentage rate)								
Commercial banks								
New cars (48 mo.)[2]	9.6	9.0	8.9	9.2	9.0	9.0	n.a.	n.a.
Personal (24 mo.)[2]	13.9	13.5	13.5	13.8	13.8	13.8	n.a.	n.a.
Credit cards[3]	16.0	15.6	15.9	15.8	15.8	15.8	n.a.	n.a.
Auto finance companies[4]								
New cars	11.2	9.8	7.6	8.0	6.3	5.9	6.1	7.3
Used cars	14.5	13.5	13.1	13.4	13.4	13.4	13.3	13.2

1. Annual data are averages of quarterly data for commercial banks and of monthly data for finance companies.
2. Average of most common rate charged for specified type and maturity during the first week of the middle month of each quarter.
3. Stated APR averaged across all credit card accounts at all reporting banks during the period.
4. Average rate for all loans of each type, regardless of maturity, made during the period.
p Preliminary. n.a. Not available.

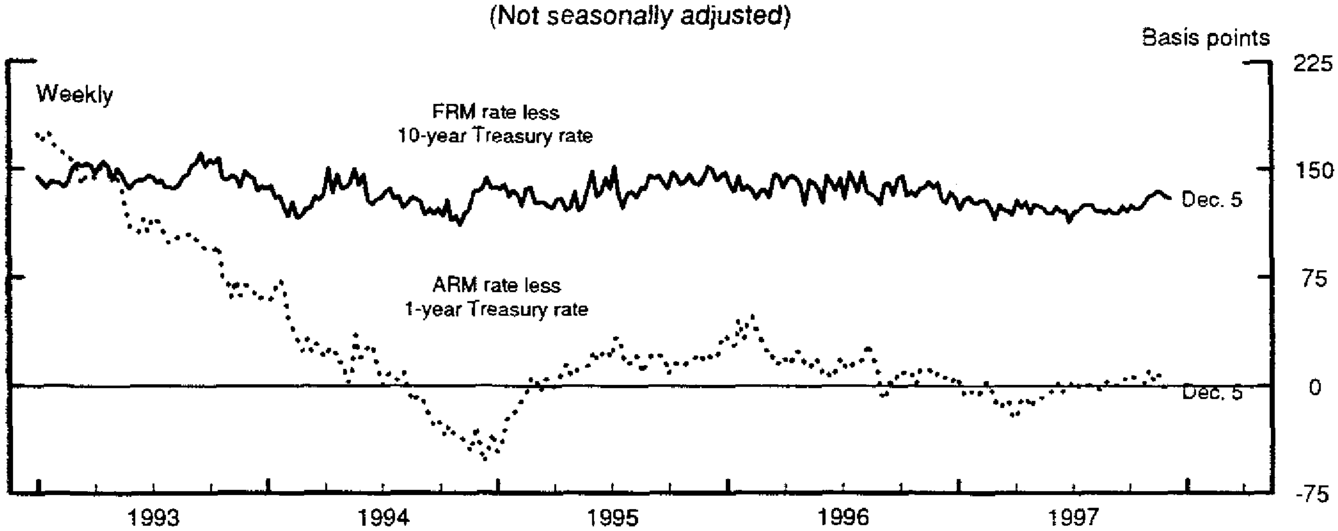
Freddie Mac FRM and ARM Rates

(Commitment rates, not seasonally adjusted)



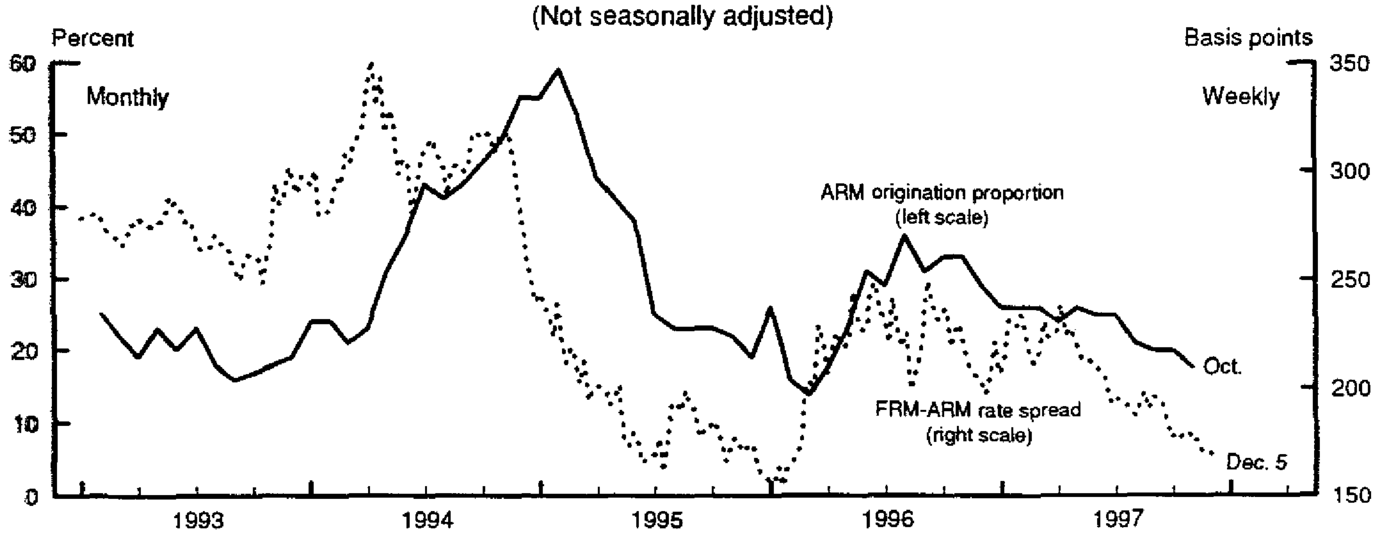
Spreads of Mortgage Rates Over Treasury Rates

(Not seasonally adjusted)



Freddie Mac FRM-ARM Spread and FHFB ARM Origination Proportion

(Not seasonally adjusted)



TREASURY FINANCING
(Billions of dollars: total for period)

Item	1997 Q1	Q2	Q3	Sept.	Oct.	Nov.[e]
Total surplus / deficit(-)	-52.0	100.1	-11.3	49.6	-35.6	--
Means of financing deficit						
Net borrowing and repayments (-)	48.0	-69.2	10.6	-18.3	6.3	28.7
Nonmarketable	4.0	1.9	4.1	3.3	7.2	3.3
Marketable	44.0	-71.1	6.5	-21.6	-0.9	25.4
Bills	7.9	-81.4	-2.2	-20.1	1.1	16.3
Coupons	36.1	10.3	8.7	-1.5	-2.1	9.1
Decrease in cash balance	-.7	-17.8	7.6	-31.5	23.4	0.5
Other[1]	4.6	-13.1	-7.0	0.3	5.9	--
Memo:						
Cash balance, end of period	33.5	51.3	43.6	43.6	20.3	19.8

Note. Details may not sum to totals because of rounding.
1. Direct loan financing, accrued items, checks issued less checks paid, and other transactions.
e Estimated.

NET CASH BORROWING OF GOVERNMENT-SPONSORED ENTERPRISES
(Billions of dollars)

Agency	1997 Q2	Q3	Aug.	Sept.	Oct.
FHLBs	23.6	5.2	0.2	3.0	-7.1
FHLMC	8.3	-1.9	4.2	-5.6	12.4
FNMA	9.3	12.5	-0.5	9.9	-19.9
Farm Credit Banks	1.2	-0.5	-0.8	0.5	-0.5
SLMA	1.7	-4.3	-0.3	-4.7	n.a.

Note. Excludes mortgage pass-through securities issued by FNMA and FHLMC.

only about 18 percent of the total conventional mortgage originations and a lowering of the ARM share of outstandings to less than 25 percent. Interest rates on FRMs have followed the decline in Treasury rates, to 7.15 percent most recently, the lowest level in almost two years and about 40 basis points above their cyclical lows in 1993.

Government Finance

The federal deficit is expected to rise in the fourth quarter, reflecting the typical seasonal pattern. The Treasury will finance most of the fourth-quarter deficit by borrowing from the public, although it is also expected to reduce its cash balance by a significant amount. In light of the continued small deficit, the Treasury has reduced auction sizes further, cutting the three-month and six-month bill auctions each by $250 million in mid-November. Part of the financing in the bill sector has taken the form of a $21 billion cash management bill that will mature after the mid-January tax receipts.

Spreading financial strains in Asia have heightened concerns in the market that foreign holders may be forced to sell some of their Treasury securities in large volume to bolster income statements by realizing profits and to fund repayment of dollar or home currency liabilities. Foreign official dollar reserves have recently leveled off, and the Federal Reserve's custody holdings for foreign central banks have declined about $25 billion from their April peak. (These custody holdings include securities financed through official currency interventions in the foreign exchange market.) However, any drop in demand from these sources seems at least to have been offset by the redirection of funds by other investors toward the safety and liquidity provided by Treasury securities as well as by perceptions of restraint on demand and prices in the United States.

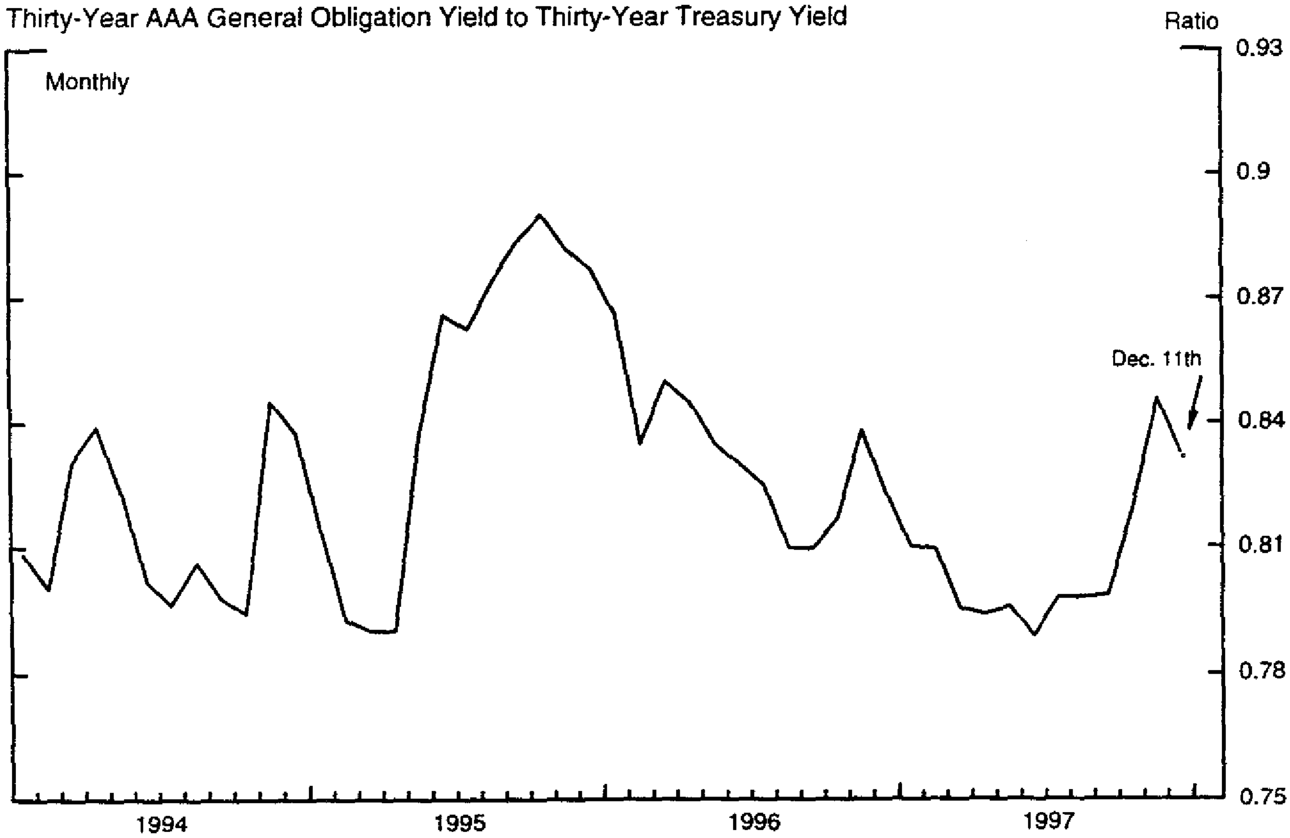
Spreads between noncallable, agency-issued securities and Treasuries have remained stable over the intermeeting period. Unlike earlier in the year, no global bond was issued, probably because the GSEs were reluctant to tap foreign financial markets at a time of turmoil abroad. The Federal Home Loan Mortgage Corporation recently guaranteed an issue of so-called CRA mortgage bonds, which are based on loans to low- and moderate-income homeowners. Purchasing such bonds will help banks satisfy requirements arising from the 1977 Community Reinvestment Act. Besides the implicit government guarantee, the lower repayment risk

GROSS OFFERINGS OF MUNICIPAL SECURITIES
(Billions of dollars; monthly rates, not seasonally adjusted)

	1994	1995	1996	1997 Q2	1997 Q3	1997 Sept.	1997 Oct.	1997 Nov.
Total tax-exempt	16.2	15.4	17.9	20.8	23.6	25.6	22.0	19.9
Long-term	12.8	12.1	14.3	16.9	17.9	20.5	18.6	16.7
Refundings[1]	4.0	3.6	4.9	4.6	8.7	11.0	7.1	5.5
New capital	8.8	8.5	9.4	12.3	9.2	9.5	11.5	11.1
Short-term	3.3	3.3	3.6	3.9	5.6	5.1	3.4	3.2
Total taxable	0.7	0.7	0.8	1.6	0.8	0.9	0.6	0.6

Note. Includes issues for public and private purposes.
1. Includes all refunding bonds, not just advance refundings.

Tax-Exempt to Taxable Yield Ratio



of such loans--since lower-income borrowers have fewer refinancing options--makes the CRA bonds attractive.

Gross offerings of long-term municipal securities dropped about $2 billion, to $16.7 billion in November, owing to a continued fall-off in refundings from their fast third-quarter pace. Yields on long-term tax exempts declined some (table), though by much less than yields on Treasuries of similar maturities (chart), and the ratio of municipal yields to taxable yields rose further.

Monetary and Credit Aggregates

The monetary aggregates grew briskly in November: M2 and M3 expanded at annual rates of 7 percent and 11 percent respectively, putting M2 just above, and M3 well above, their annual ranges. Rather than extending its trend decline, M1 grew near an 8 percent annual rate last month, reflecting the unusually rapid expansion of currency and demand deposits. Some of this increase in currency was attributable to shipments to Russia. Demand deposits also surged, boosted by a slight, probably temporary slowdown in the introduction of new sweeps and a pickup in mortgage refinancing induced by the decline in longer-term rates last month. (Funds used to prepay existing mortgages are sometimes temporarily held in escrow in these accounts.)

M2 growth provided a boost to M3, which was amplified by a substitution of managed liabilities in M3 for other sources of funds. The growth of large time deposits ticked up to a 12-1/2 percent pace in November, while RPs almost doubled at an annual rate. Banks apparently had more assets to fund last month, judging by the expansion of bank credit.

Bank credit, adjusted for the effects of mark-to-market accounting rules, grew at an annual rate of 11-1/2 percent in November, a rapid pace in line with that of the previous two months and well above that of earlier in 1997. In particular, commercial banks significantly expanded their securities portfolio in November, which contributed to the growth of bank credit and probably boosted the growth of RPs. This expansion in the securities portfolio mainly occurred at large domestic and foreign banks and was apparent in both government and other securities.

Business loan growth slowed from a 10 percent rate in October to a 5-1/4 percent pace in November, even though banks remain vigorous in their pursuit of C&I loans: In the third-quarter bank examiner survey, for instance, respondents by a wide margin

MONETARY AGGREGATES
(Based on seasonally adjusted data)

Aggregate or component	1996	1997 Q2	1997 Q3	1997 Sept	1997 Oct.	1997 Nov. (p)	1996:Q4 to Nov. 97 (p)	Level (bil. $) Nov. 97 (p)
Aggregate	Percentage change (annual rate)[1]							
1. M1	-4.6	-5.5	0.2	-9.9	-3.8	7.7	-1.5	1064.2
2. M2[2]	4.3	3.8	5.1	5.9	4.8	6.8	5.2	3998.3
3. M3	6.6	6.7	8.4	9.5	8.1	10.7	8.4	5291.8
Selected components								
4. Currency	5.7	5.8	6.7	9.6	7.5	10.9	7.4	421.8
5. Demand deposits	2.8	-6.7	0.1	-34.0	-12.9	14.0	-2.5	390.9
6. Other checkable deposits	-23.1	-20.4	-10.3	-2.4	-9.2	-7.8	-12.6	243.2
7. M2 minus M1[3]	8.4	7.4	6.9	11.8	7.9	6.5	7.9	2934.1
8. Savings deposits	11.7	9.3	6.1	13.7	11.9	8.1	9.6	1379.5
9. Small time deposits	1.4	2.5	3.9	2.2	2.7	0.1	2.4	966.6
10. Retail money market funds	14.5	11.4	14.0	23.9	7.3	12.8	13.9	588.0
11. M3 minus M2[4]	15.5	16.7	19.7	21.0	18.4	23.2	19.5	1293.6
12. Large time deposits, net[5]	16.6	20.3	25.5	29.5	7.6	12.5	19.6	580.5
13. Institution-only money market mutual funds	19.8	12.5	21.3	35.4	22.7	3.8	18.2	346.4
14. RPs	4.5	4.2	9.3	-16.7	69.4	88.2	19.7	233.6
15. Eurodollars	21.5	33.4	9.0	9.0	-25.0	13.7	22.4	133.1
Memo								
16. Sweep-adjusted M1[6]	5.1	4.1	6.0	3.1	3.5	8.9	5.9	1312.3
17. Monetary base	3.8	3.2	6.1	7.5	6.6	11.7	6.0	476.6
18. Household M2[7]	4.5	5.0	5.9	9.2	6.8	5.9	6.2	3607.2
	Average monthly change (billions of dollars)[8]							
Memo								
Selected managed liabilities at commercial banks:								
18. Large time deposits, gross	8.5	11.3	12.7	12.0	4.3	7.9	...	672.4
19. Net due to related foreign institutions	-2.0	2.7	-5.2	-0.5	-19.2	-1.2	...	186.1
20. U.S. government deposits at commercial banks	0.0	2.5	-3.3	1.1	3.6	-2.1	...	20.0

1. For the years shown, fourth quarter-to-fourth quarter percent change. For the quarters shown, based on quarterly averages.
2. Sum of seasonally adjusted M1, retail money market funds, savings deposits, and small time deposits.
3. Sum of retail money funds, savings deposits, and small time deposits, each seasonally adjusted separately.
4. Sum of large time deposits, institutional money funds, RP liabilities of depository institutions, and Eurodollars held by U.S. addressees, each seasonally adjusted separately.
5. Net of holdings of depository institutions, money market mutual funds, U.S. government, and foreign banks and official institutions.
6. Sweep figures used to adjust these series are the estimated national total of transaction account balances initially swept into MMDAs owing to the introduction of new sweep programs, on the basis of monthly averages of daily data.
7. M2 less demand deposits
8. For the years shown, "average monthly change" is the fourth quarter-to-fourth quarter dollar change, divided by 12. For the quarters shown, it is the quarter-to-quarter dollar change, divided by 3.

p--Preliminary.

Commercial Bank Credit
(Percent change; seasonally adjusted annual rate)

Type of credit	1996	1997 Q2	1997 Q3	1997 Sep	1997 Oct	1997 Nov p	Level, Nov 1997 p (billions of $)
1. Bank credit: Reported	4.0	7.7	6.9	7.5	10.5	13.6	4,076.6
2. Adjusted[1]	4.5	9.4	6.0	10.8	10.5	11.5	3,982.0
3. Securities: Reported	-1.6	2.3	4.1	7.6	16.5	40.5	1,080.9
4. Adjusted[1]	0.0	8.9	0.3	21.2	17.0	34.2	986.3
5. U.S. government	-0.8	9.7	-0.5	14.8	13.1	22.0	745.4
6. Other[2]	-3.4	-14.8	15.6	-8.9	24.6	83.8	335.5
7. Loans[3]	6.1	9.6	7.9	7.5	8.5	4.2	2,995.7
8. Business	8.6	8.4	9.0	17.6	9.9	5.3	848.3
9. Real estate	4.1	12.3	9.2	8.5	5.3	5.7	1,225.3
10. Home equity	6.3	20.5	16.8	15.3	6.3	15.0	97.1
11. Other	3.9	11.6	8.6	7.9	5.4	4.9	1,128.3
12. Consumer: Reported	5.5	-2.8	0.6	-7.9	-13.7	1.9	510.2
13. Adjusted[4]	10.7	0.5	3.4	7.2	5.1	12.2	715.2
14. Other[5]	7.9	21.5	11.4	3.9	43.8	0.0	411.9

Note. Adjusted for breaks caused by reclassifications. Monthly levels are pro rata averages of weekly (Wednesday) levels. Quarterly levels (not shown) are simple averages of monthly levels. Annual levels (not shown) are levels for the fourth quarter. Growth rates shown are percentage changes in consecutive levels, annualized but not compounded.

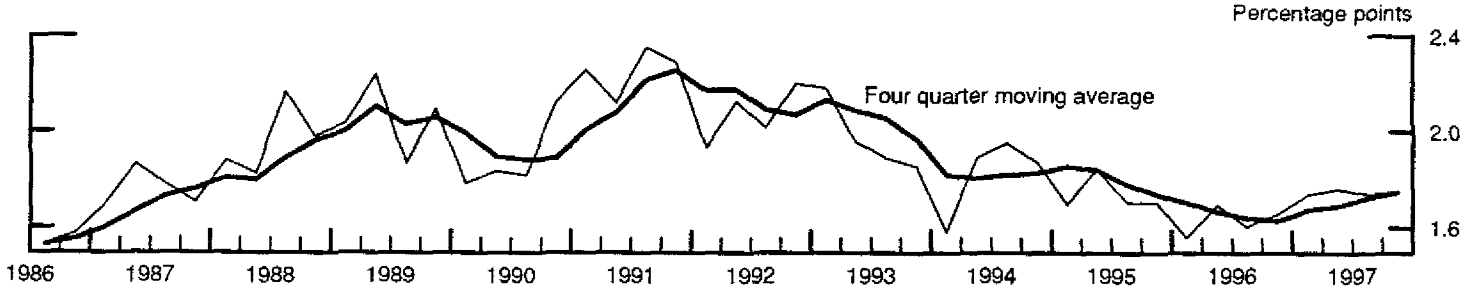
1. Adjusted to remove effects of mark-to-market accounting rules (FIN 39 and FASB 115).
2. Includes securities of corporations, state and local governments, and foreign governments and any trading account assets that are not U.S. government securities.
3. Excludes interbank loans.
4. Includes an estimate of outstanding loans securitized by commercial banks.
5. Includes security loans, loans to farmers, state and local governments, and all others not elsewhere classified. Also includes lease financing receivables.

p Preliminary.

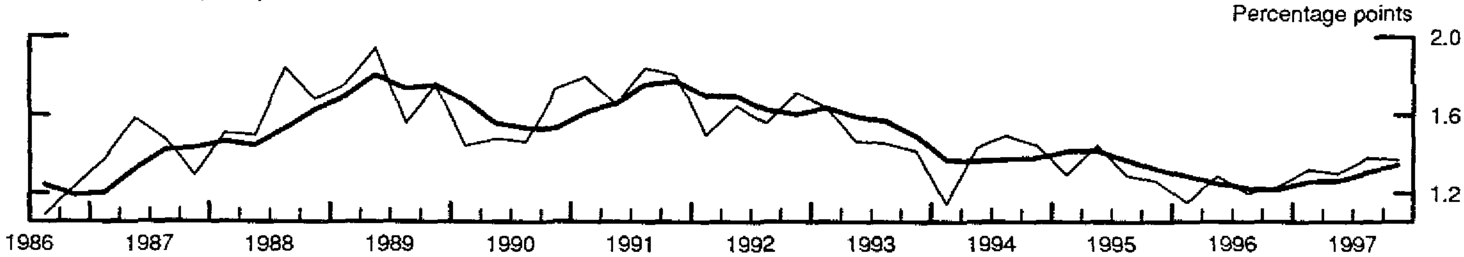
Commercial and Industrial Loan Rates

(Spreads over intended federal funds rate, by loan size)

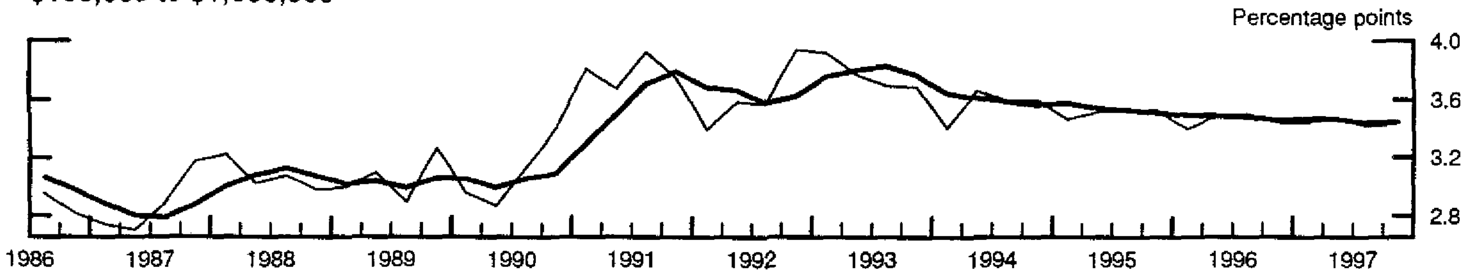
All Loans



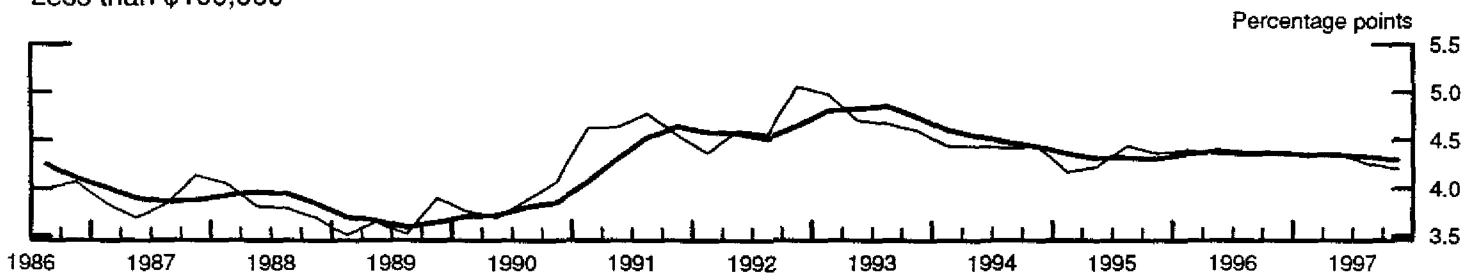
More than $1,000,000



$100,000 to $1,000,000



Less than $100,000



Source. Survey of Terms of Business Lending, domestic banks. The most recent quarterly survey occurred November 3-7.

identified that category as the one in which terms and standards had been eased the most. The most recent survey of bank lending terms indicates that spreads on business loans edged lower in the fourth quarter (chart). According to the survey, spreads are a bit higher than one year ago for loans greater than $1,000,000, probably reflecting a shift toward riskier loans; spreads on smaller loans are lower on net.

Despite strains in Japan, credit extended by Japanese branches and agencies has remained about flat of late. While real estate loans at those entities have continued to run off, their business lending has picked up the slack.

APPENDIX
REVIEW OF DEBT AND MONEY IN 1997

Summary

Growth of the total debt of domestic nonfinancial sectors slowed in 1997, but that of M2 and M3 picked up. The decline in the growth of total debt reflected a sharply reduced expansion of federal debt owing to the smaller fiscal deficit. Nonfederal debt grew at the same rate as last year, as a deceleration of household debt matched a slight acceleration of business debt and a more noticeable pickup in state and local debt. Strong growth in depository credit--particularly bank credit--contributed to rapid expansion in M3. With opportunity costs little changed, M2 expanded at roughly the same rate as nominal GDP.

Domestic Nonfinancial Debt

Domestic nonfinancial debt advanced at a 4-1/2 percent rate through October, notably slower than nominal GDP but near the middle of its monitoring range. Federal debt grew less than 1 percent this year, down from 3-3/4 percent last year. The fiscal 1997 deficit was below that of any year since 1974. Nonfederal debt grew at a 5-3/4 percent rate.

Household Finance. After slowing by nearly half in 1996, growth in consumer credit edged down further this year. This moderation occurred despite a pickup in consumer outlays and likely reflected a more cautious attitude toward credit use by households, substitution of home mortgage borrowing for consumer credit, and a more restrictive posture by bank lenders toward some borrowers. The delinquency rate on banks' consumer loans seems to have plateaued this year, albeit at a high level, but the charge-off rate rose to new highs, and personal bankruptcies continued to increase rapidly through the first half of the year before stabilizing in the third quarter.

In contrast, substitutions of real estate loans for consumer loans and robust growth in residential structures bolstered total home mortgage growth, although the pace was a bit lower than last year. At banks, home equity lending expanded at a double-digit pace as banks reportedly encouraged customers to use this source of funds to consolidate their credit card debt. More dramatically, other lenders, particularly finance companies, have been aggressively offering mortgages with loan-to-value ratios of 100 percent or more as a means of consolidating other debt. The home equity and nonbank mortgage market were undergirded by a strong appetite by investors for securities collateralized by these loans. Delinquency and charge-off rates on home mortgage loans, including home equity loans, remained low.

Business Finance. Business debt expanded at a fairly rapid 6 percent rate this year, up a bit from last year. A surge in capital outlays outpaced a hefty advance in internal funds, and merger-related equity retirements remained brisk. With this year's appreciable business borrowing, the deleveraging of nonfinancial corporations' balance sheets that has been going on since the early 1990s has about stopped. Measures of the financial condition of the business sector, on balance, were favorable. Upgrades of corporate debt about matched downgrades, and bond defaults. C&I delinquency rates, and charge-off rates all remained low; in contrast, business bankruptcies rose somewhat, albeit from a low level. Credit markets continued to be quite receptive to new debt offerings, as corporate bond spreads stayed near historical lows, widening only modestly during the financial turbulence this fall. Banks also continued to be willing lenders, reporting further reductions in spreads of loan rates over benchmark rates. The gross issuance of bonds by nonfinancial corporations through November was more than a third higher than in 1996; junk bonds accounted for an unusually large part of the increase. Gross issuance of equity also was strong, but net issuance remained deeply negative because of merger-related retirements and a large volume of stock buybacks by corporations.

Commercial mortgages grew moderately for the second consecutive year, as prices and activity in commercial building continued to strengthen. Banks were the largest source of funds for these loans. Another significant source of funds was commercial-mortgage-backed securities, and their popularity likely held down real estate loan growth at banks. Indeed, increases this year, through September, in securities backed by all types of income property mortgages, including multifamily, nearly equaled increases in the outstanding amount of these loans on banks' books.

State and Local Finance. State and local debt expanded a little more than 5 percent in 1997, after leveling out last year following two years of declines. Municipal debt outstanding had been held down in recent years by the retirement of bonds that were advanced refunded in the early 1990s, but this factor has become much less pronounced because advance-refunded debt was largely worked down by the end of 1996.

Depository credit

Credit extended by depository institutions expanded at a 6-1/4 percent pace through November, up appreciably from last year. Bank credit accelerated to an 8-1/4 percent pace, owing in part to the acquisition of thrifts by banks. The increase in bank credit was the fastest in ten years, and banks' share of domestic nonfinancial debt outstanding climbed to its highest level since 1988. Bank credit accelerated in part because banks accumulated securities--which had run off in 1995 and had been flat in 1996--at a brisk pace in 1997. Loans also advanced a bit more quickly this year than last, though more slowly than in 1995.

The solid growth in bank loans occurred despite a net decline in consumer loans that owed to sharply slower growth in loans originated by banks and continued robust securitizations. Real estate loans at banks, by contrast, have grown at nearly twice the pace posted in 1996. This category of credit has benefited from the rapid growth in home equity lines, the turnaround in commercial real estate lending, an acceleration in home mortgages, and thrift acquisitions.

C&I loan expansion was strong this year, partly because of the factors boosting business borrowing in general but also because banks increased their share of the business credit market. Mergers and acquisitions picked up among middle-market firms, which are more likely than large corporations to use bank financing. In addition, banks continued to compete vigorously for business loans, narrowing spreads and easing other terms. To date, however, Senior Loan

Officer Surveys have found little evidence that banks are easing standards on these loans, and C&I loan charge-off and delinquency rates remain extremely low.

Continued high profitability and abundance of capital facilitated an aggressive position by banks. Certainly, some banks faced credit quality problems on their consumer loans, which led to consolidation of a few credit card lenders. But overall delinquency and charge-off rates stayed quite low, and banks' return on equity remained in the elevated range it has occupied for several years.

Like banks, thrifts are profitable and well capitalized, and they also were actively pursuing borrowers in 1997. The slowing in thrift credit growth reflected the acquisition of thrifts by commercial banks: Among thrifts not acquired during the year, assets grew roughly 8 percent.

Monetary aggregates

Boosted in part by the solid growth in depository credit, M3 shot up this year, expanding 8-1/2 percent through November, well above its 2 to 6 percent annual range. M3 was augmented by a funding shift, concentrated at U.S. branches and agencies of foreign banks, from borrowings from related offices abroad, which are not included in M3, to large time deposits issued in the United States, which are. Another factor contributing to the strength in M3 was the increasing inroads made by institution-only money funds in corporate cash management.

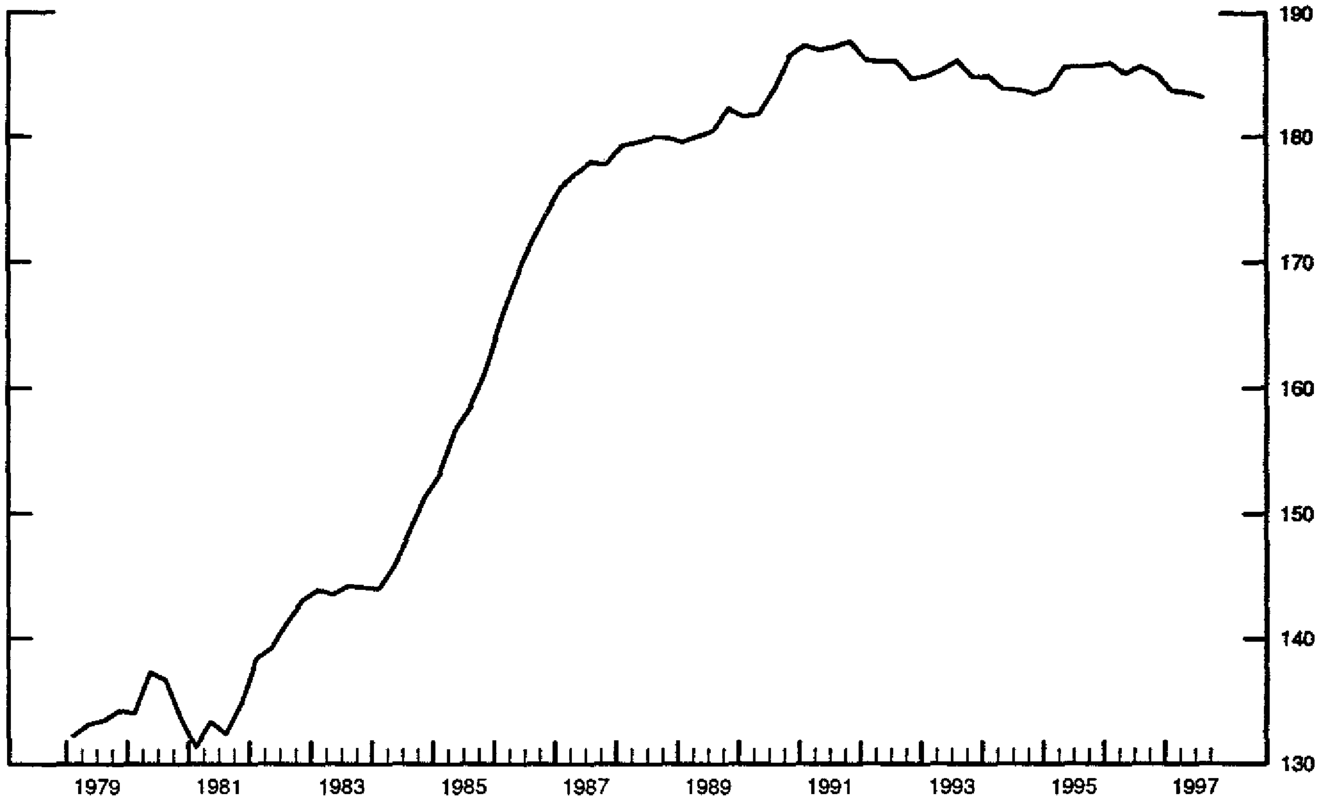
While not matching the strong pace of M3, M2 grew at a healthy 5-1/4 percent rate through November, a touch above its 1 to 5 percent annual range. Even though the opportunity cost of holding M2 was about unchanged over the year, M2 appears to have grown a little more slowly than nominal GDP, continuing the upward drift in velocity that has occurred for the past few years. The ongoing adoption of sweep programs by banks again resulted in considerable growth in the savings and MMDAs component of M2 at the expense of transactions accounts. The initiation of programs that sweep funds out of NOW accounts appears to be slowing, but retail demand deposit sweeps have picked up, leaving the total amount by which sweep account balances increased similar to last year. Inflows to M2 money funds picked up toward year-end, probably in response to the turbulence in the stock market. Indeed, inflows into bond and stock mutual funds did slow a bit in November, but 1997 could well be a record year for these funds. Currency growth was strong, boosting M2 expansion. Shipments of currency abroad, while still elevated, were off a bit from the extraordinary levels seen in recent years, but the effects of strong domestic spending were more than offsetting.

THE GROWTH AND FLOW OF MONETARY AND CREDIT AGGREGATES
(Q4 to Q4 averages, seasonally adjusted unless otherwise noted)

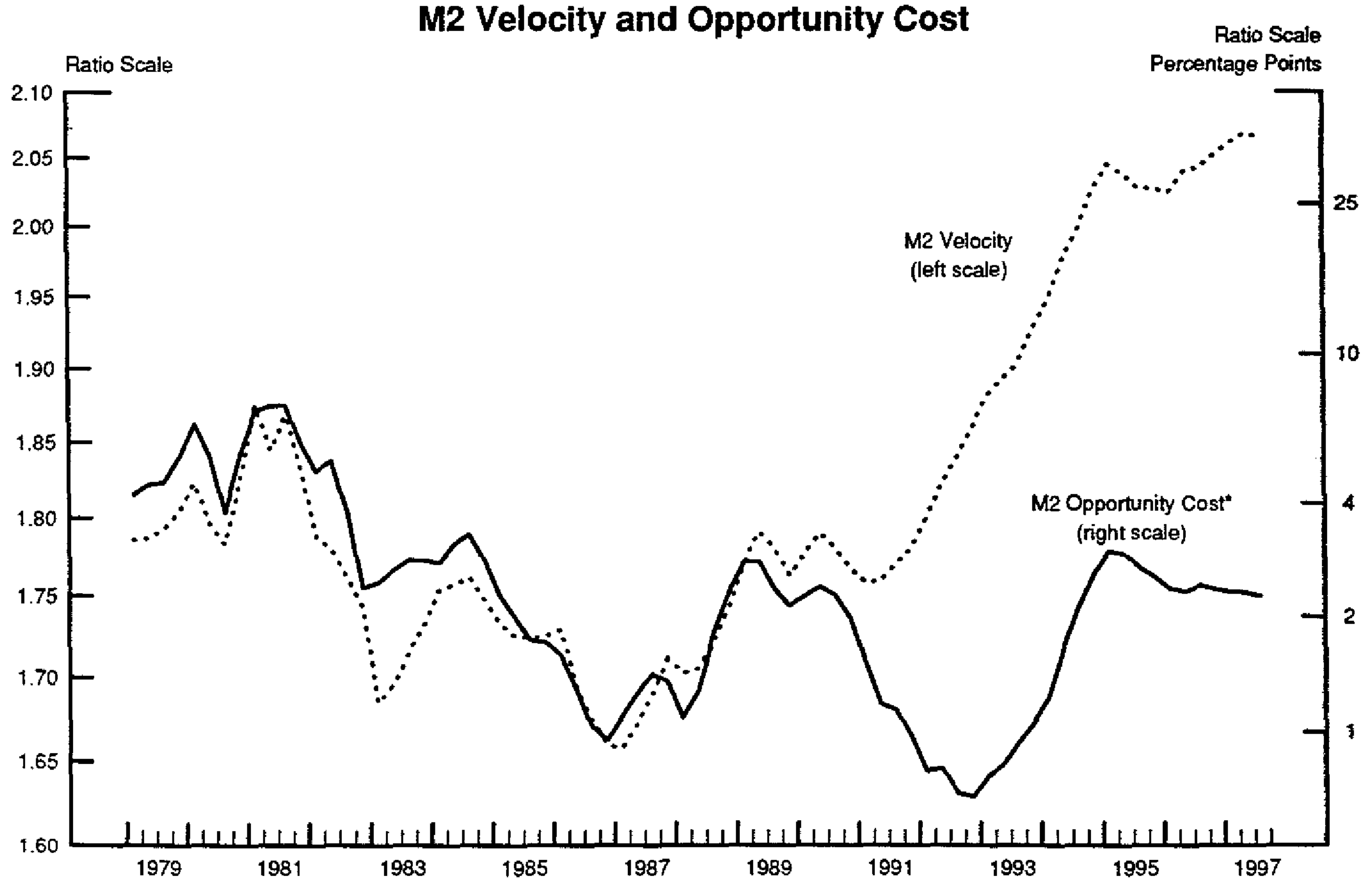
	Growth rates or flows	1993	1994	1995	1996	1997[1]	Memo: Recent 1997 levels (billions of dollars)[1]
Growth rates (percent)							
	Domestic nonfinancial debt - total	5.1	5.1	5.4	5.2	4.4	15,007.8
	Federal	8.4	5.7	4.4	3.7	0.6	3,789.6
	Nonfederal	4.0	4.8	5.7	5.7	5.7	11,218.2
	Depository credit	3.5	5.1	5.6	4.3	6.3	5,131.1
	Bank credit[2]	5.0	6.0	7.1	4.5	8.2	3,974.4
	Thrift credit	-0.2	2.6	1.6	3.6	0.8	1,229.4
	M1	10.6	2.5	-1.6	-4.6	-1.5	1,064.2
	Sweep-adjusted M1[3]	10.6	3.3	1.6	5.1	5.9	1,312.3
	M2	1.3	0.6	4.0	4.3	5.2	3,998.3
	M3	1.1	1.7	6.1	6.6	8.4	5,291.8
	Memo: Nominal gross domestic product	5.0	5.8	4.0	5.6	5.7	8,128.8
Flows ($ billions, December to December)							
	Currency	29.3	32.2	18.2	22.6	29.0	421.8
M1	Transactions deposits	75.8	-11.8	-40.3	-70.2	-47.2	634.1
	Sweep-adjusted transactions deposits[3]	75.8	-2.0	3.6	43.4	40.9	n.a.
	Nontransactions M2	-52.3	-5.4	174.6	212.2	213.7	2,934.1
M2	Savings, MMDAs, and small time deposits	-53.7	-34.8	103.7	145.9	141.2	2,346.1
	Retail MMMFs	1.4	29.4	70.9	66.3	72.5	588.0
	Non-M2 component	11.4	57.5	112.2	161.2	212.6	1,293.6
	Institution-only MMMFs	2.0	-11.0	48.4	52.4	51.4	346.4
M3	Large time deposits	-20.1	29.7	56.8	71.7	97.1	580.5
	Total RPs and Eurodollars, net (NSA)	28.3	37.2	6.0	36.1	67.1	365.0

1. For debt aggregates, the rate reported is for 1996 Q4 through October at an annual rate; for the monetary and credit aggregates, the rate reported is for 1996 Q4 through November at an annual rate; for nominal gross domestic product the rate is for 1996 Q4 to 1997 Q3 at an annual rate; depository and thrift credit data are partially projected.
2. Adjusted for the estimated effects of mark-to-market accounting rules.
3. Sweep figures used to adjust this series are the estimated national total of transaction account balances initially swept into MMDAs by new sweep programs, on the basis of monthly averages of daily data.

Total Nonfinancial Domestic Debt as a Percent of Nominal Gross Domestic Product



M2 Velocity and Opportunity Cost



* Two-quarter moving average.

INTERNATIONAL DEVELOPMENTS

U.S. International Trade in Goods and Services

In September, the deficit in U.S. international trade in goods and services widened, as exports declined and imports rose. For the third quarter, the deficit was significantly larger than that recorded in the second quarter, but not much larger than the deficit in the first quarter. Trade data for October will be released on December 18.

NET TRADE IN GOODS & SERVICES
(Billions of dollars, seasonally adjusted)

	1996	Annual rates 1997 Q1	Q2	Q3	Monthly rates 1997 Jul	Aug	Sep
Real NIPA 1/							
Net exports of G&S	-114.4	-126.3	-136.6	-160.0	...	...	...
Nominal BOP							
Net exports of G&S	-111.0	-117.2	-102.6	-118.5	-10.0	-9.5	-11.1
Goods, net	-191.2	-199.1	-188.5	-206.2	-16.8	-16.6	-18.1
Services, net	80.1	82.0	85.9	87.7	6.8	7.1	7.1

1. In billions of chained (1992) dollars.
Source. U.S. Dept. of Commerce, Bureaus of Economic Analysis and Census.

Exports of goods and services in the third quarter were only marginally higher than those in the second quarter. Increased exports of machinery, industrial supplies, and higher service receipts (half from foreign travelers in the United States and half from other private services) were nearly offset by sharp drops in exports of aircraft and gold. By region, increases in shipments to Mexico and other Latin American countries were more than offset by small declines in exports to most other areas (including Japan and other countries in Asia).

Imports of goods and services in the third quarter were 1-1/2 percent higher compared with the second quarter. There were increases in most major trade categories; the exceptions were imports of gold and petroleum products.

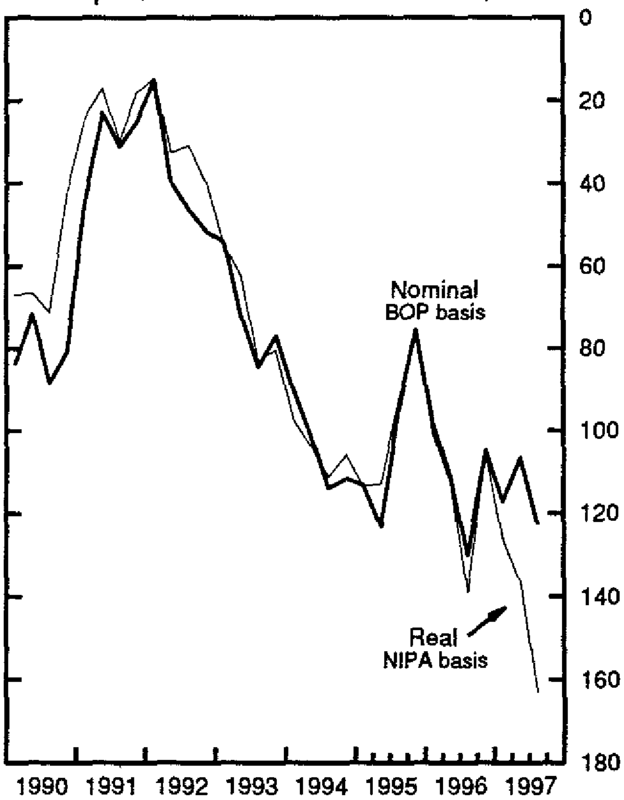
Oil Imports and Prices

The quantity of imported oil increased again in the third quarter relative to the second quarter, marking two consecutive quarters of strong increases in oil imports. These relatively high import levels were driven by extremely robust consumption in the

U.S. International Trade in Goods and Services

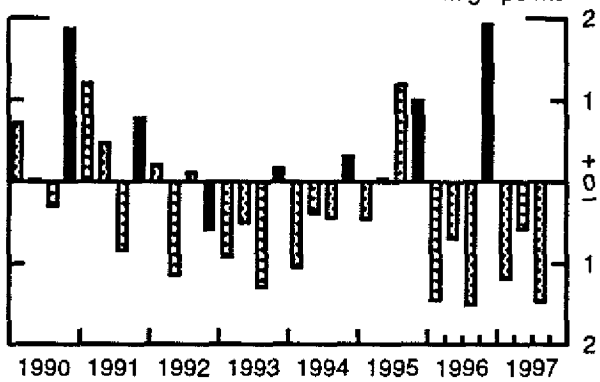
Net Exports

Billions of dollars, SAAR

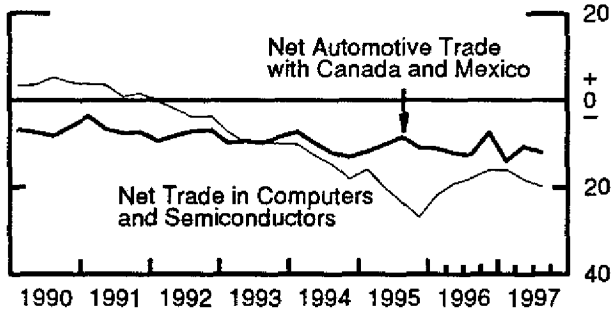


Contribution of Net Exports to Real GDP Growth

Percentage points

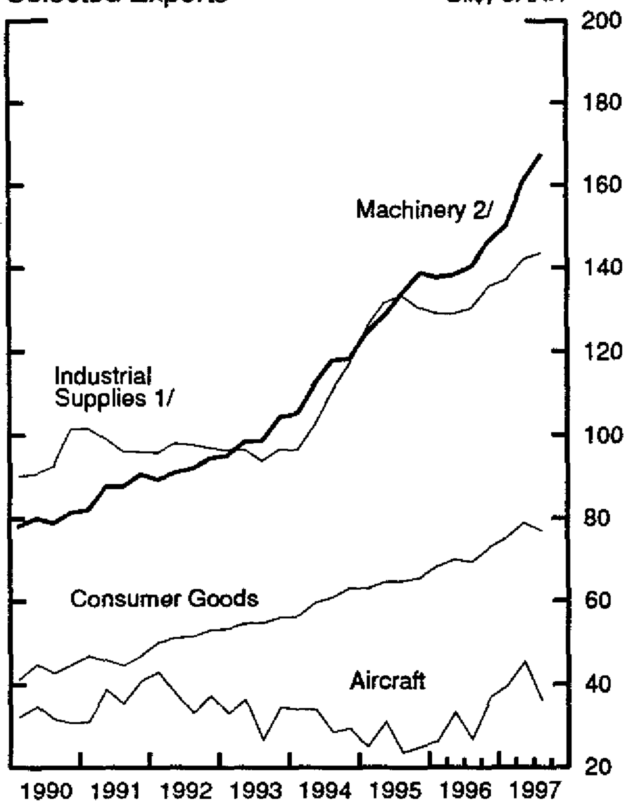


Bil$, SAAR



Selected Exports

Bil$, SAAR

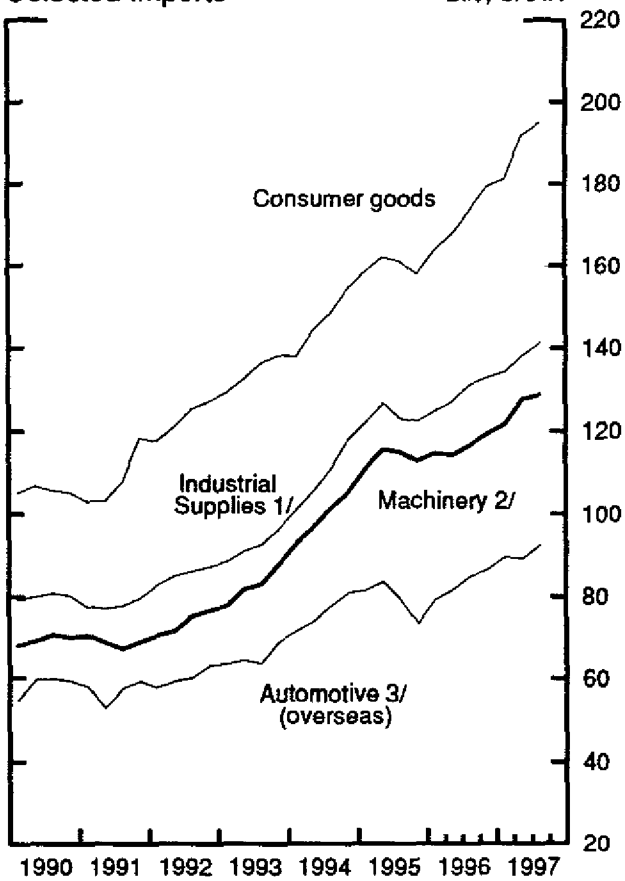


1/ Excludes agriculture and gold.

2/ Excludes computers and semiconductors.

Selected Imports

Bil$, SAAR



1/ Excludes oil and gold.

2/ Excludes computers and semiconductors.

3/ Excludes Canada and Mexico.

U.S. EXPORTS AND IMPORTS OF GOODS AND SERVICES
(Billions of dollars, SAAR, BOP basis)

	Levels				Amount Change 1/			
	1997		1997		1997		1997	
	Q2	Q3	Aug	Sep	Q2	Q3	Aug	Sep
Exports of G&S	939.0	940.0	942.9	936.0	41.9	1.0	9.5	-6.9
Goods exports	685.6	682.3	687.9	678.1	35.5	-3.3	7.0	-9.8
Agricultural	56.4	58.1	59.5	60.3	-0.9	1.7	4.9	0.9
Gold	9.3	3.4	3.4	3.6	2.6	-5.8	-0.0	0.2
Other goods	619.9	620.7	625.1	614.2	33.8	0.8	2.1	-10.9
Aircraft & pts	45.5	36.2	32.2	35.2	5.8	-9.2	-9.1	3.0
Computers	50.1	52.5	53.4	51.9	3.8	2.3	1.2	-1.5
Semiconductors	38.3	40.3	40.4	41.1	0.5	2.0	0.9	0.7
Other cap gds	163.0	169.5	173.0	169.5	10.8	6.5	7.1	-3.6
Automotive	73.4	73.3	74.1	70.5	2.5	-0.2	-1.0	-3.6
to Canada	38.5	38.8	40.0	37.0	-0.2	0.3	0.5	-3.1
to Mexico	11.3	11.3	10.8	12.5	0.9	-0.0	0.4	1.7
to ROW	23.6	23.1	23.2	21.0	1.8	-0.4	-1.9	-2.2
Ind supplies	142.1	143.6	145.3	142.9	5.0	1.5	2.6	-2.3
Consumer goods	78.9	77.0	77.4	76.8	3.6	-1.9	0.6	-0.6
All other	28.6	28.4	29.4	26.2	1.8	-0.2	2.3	-3.2
Services exports	253.3	257.6	255.0	257.9	6.4	4.3	2.5	2.9
Imports of G&S	1041.5	1058.5	1056.4	1068.8	27.5	17.0	2.8	12.4
Goods imports	874.2	888.5	886.6	895.8	24.9	14.3	3.5	9.2
Petroleum	71.0	70.1	70.9	72.5	-5.7	-0.9	3.9	1.6
Gold	11.0	3.0	2.6	3.3	2.3	-8.0	-0.4	0.7
Other goods	792.2	815.4	813.1	820.0	28.3	23.2	-0.1	6.9
Aircraft & pts	15.5	18.8	17.8	18.3	1.9	3.3	-2.6	0.5
Computers	70.5	73.6	74.6	74.0	5.1	3.0	2.5	-0.7
Semiconductors	36.1	39.0	39.5	39.3	1.4	2.9	1.4	-0.2
Other cap gds	129.6	130.8	132.8	131.3	6.1	1.2	4.6	-1.5
Automotive	138.3	143.5	141.8	141.2	-3.9	5.2	-5.7	-0.6
from Canada	49.2	50.8	49.9	48.0	-3.5	1.7	-4.6	-1.9
from Mexico	26.0	25.5	25.4	27.1	1.8	-0.5	1.3	1.7
from ROW	63.2	67.2	66.5	66.2	-2.2	4.0	-2.4	-0.3
Ind supplies	138.1	141.1	141.0	142.9	3.9	3.0	1.5	2.0
Consumer goods	192.0	194.9	192.1	199.3	10.8	2.8	-1.1	7.2
Foods	39.9	40.5	40.2	40.6	1.9	0.6	-0.6	0.4
All other	32.1	33.2	33.3	33.0	1.2	1.1	-0.0	-0.3
Services imports	167.4	170.0	169.8	173.0	2.4	2.6	-0.7	3.2
Memo:								
Oil qty (mb/d)	10.80	10.92	10.90	11.22	0.95	0.12	0.25	0.32
Oil price ($/bbl)	18.01	17.57	17.81	17.70	-3.34	-0.44	0.60	-0.11

1. Change from previous quarter or month.
Source. U.S. Dept. of Commerce, Bureaus of Economic Analysis and Census.

second and third quarters--up more than three percent from rates observed a year ago. Preliminary Department of Energy statistics indicate that oil imports remained strong in October due to continued high consumption demand.

The price of imported oil rose 5 percent in October after declining 1/2 percent in September. Tensions in the Middle East--that led to a buildup of U.S. forces in the Persian Gulf and a perceived threat to oil supplies from the region--contributed to the jump in October prices. On balance, import prices have moved relatively little since April of this year.

The spot price for WTI rose $1.47 per barrel in October, averaging $21.26 per barrel and reflecting increased tensions in the Middle East. Prices declined $1.09 per barrel in November, when the United States field commander explained that U.S. forces had no intention of engaging in armed conflict with Iran and dropped further when the Persian Gulf coalition partners announced that force would be used against Iraq as a last resort. Prices have been pushed even lower in December in reaction to OPEC's announcement of a nearly 10 percent increase in its production quota. Spot WTI is currently trading below $19 per barrel for the first time since January 1996.

Prices of Non-oil Imports and Exports

Non-oil import prices continued their downward trend in October-November, but at a somewhat faster rate than in the third quarter. Most of the declines were in foods, computers, semiconductors, and other capital goods. In contrast, prices of imported automotive products rose.

Export prices decreased moderately in October-November. The declines were primarily attributable to lower prices for agricultural products, other industrial supplies, and capital goods. Increased prices were recorded for exports of automotive products and consumer goods.

U.S. Current Account

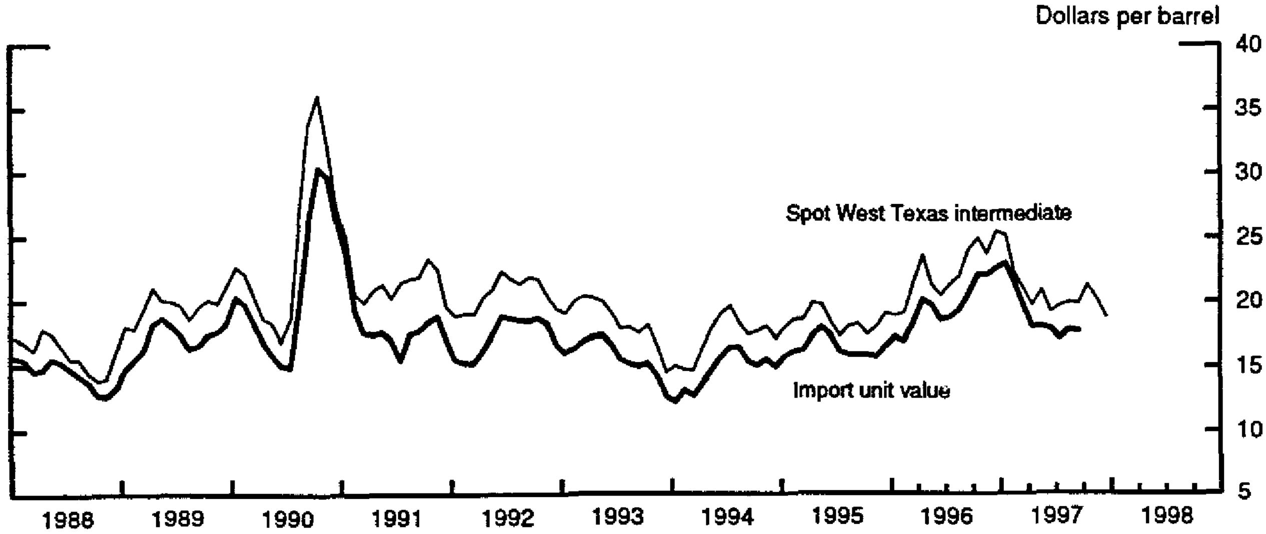
The U.S. current account deficit widened $17.2 billion (SAAR) in the third quarter. A larger deficit for net goods and services accounted for most of the change from second to third quarters. Only small changes were recorded for investment income and transfers.

PRICES OF U.S. IMPORTS AND EXPORTS
(Percentage change from previous period)

	Annual rates 1997			Monthly rates 1997		
	Q2	Q3	Q4e/	Sep	Oct	Nov
	----------BLS prices (1995=100)----------					
Merchandise imports	-8.8	-1.5	-0.6	-0.1	0.1	-0.3
Oil	-48.5	-2.9	17.1	0.1	4.0	-1.5
Non-oil	-3.4	-1.6	-2.1	-0.1	-0.3	-0.1
Foods, feeds, bev.	7.9	-5.3	-4.2	0.4	-0.8	-0.9
Ind supp ex oil	-6.0	1.6	-0.9	0.4	-0.5	0.1
Computers	-17.6	-14.5	-18.4	-1.2	-3.3	-0.4
Semiconductors	-2.2	-5.3	-8.9	-0.8	-0.8	-1.7
Cap. goods ex comp & semi	-3.8	-1.1	-1.8	-0.3	-0.2	0.1
Automotive products	-0.7	1.7	1.2	0.1	0.2	0.0
Consumer goods	-1.3	-0.8	-0.4	-0.2	0.2	-0.2
Merchandise exports	-0.4	-1.1	-2.4	-0.3	-0.4	0.0
Agricultural	-0.8	-10.8	-5.6	-0.1	-1.8	0.8
Nonagricultural	-0.1	-0.1	-1.8	-0.3	-0.2	-0.1
Ind supp ex ag	1.3	0.7	-4.3	-0.4	-0.5	-0.3
Computers	-10.4	-7.9	-5.1	-0.5	-0.9	-0.2
Semiconductors	-2.7	-8.7	-13.8	-3.4	-1.1	-0.2
Cap. goods ex comp & semi	1.0	0.5	-0.3	-0.3	0.1	0.0
Automotive products	1.4	0.5	0.1	-0.1	0.1	0.0
Consumer goods	0.1	1.7	1.4	0.4	0.1	0.0
	---Prices in the NIPA accounts (1992=100)--					
Chain-weight						
Imports of gds & serv.	-7.6	-2.8	n.a.	...	...	...
Non-oil merchandise	-3.9	-2.3	n.a.	...	...	...
Exports of gds & serv.	-0.7	-1.9	n.a.	...	...	...
Nonag merchandise	-2.4	-2.3	n.a.	...	...	...

e. Average of two months.

Oil Prices



The balance on goods and services weakened $16 billion (SAAR) in the third quarter. Exports of goods and services rose only marginally following three quarters of strong growth. Imports increased 1-1/2 percent with the rise spread over most trade categories.

For investment income in the third quarter, there was a small decline in net direct investment income receipts (payments rose more than receipts rose) that was largely offset by a small strengthening in net portfolio income payments (private receipts from abroad rose more than U.S. income payments to foreigners rose).

U.S. International Financial Transactions

The fallout from the turmoil in Asian financial markets is apparent in the data on U.S. international transactions in October. Reflecting a flight to quality, private foreigners bought net more than $30 billion in U.S. Treasury securities (line 4a on the Summary of U.S. International Transactions table). As usual, the bulk of these sales was to the United Kingdom, with the identity of the ultimate purchaser unknown. However, it was also reported that residents of Japan, Mexico, and Hong Kong made large direct net purchases. In addition, private foreigners purchased net over $7 billion in U.S. government agency bonds (included in line 4b); Japanese residents accounted for about $4.5 billion of this total. Foreign net purchases of U.S. corporate stocks (line 4c) declined from the August and September pace, but remained relatively strong despite the market dip. Increases in foreign holdings of U.S. currency also have picked up in recent months (line 8).

U.S. net purchases of foreign bonds (line 5a) dropped sharply in October, while net purchases of foreign stocks (line 5b) recovered somewhat. Net purchases of securities in Europe more than accounted for the total.

Banks in the United States continued to report net outflows in October (line 3). The reported outflow was more than accounted for by transactions between U.S. branches of foreign banks and their parents. These outflows appear to reflect in part borrowing in the United States through RP transactions by a Japanese financial institution. Countering these outflows slightly, liabilities of Mexico have been increasing in recent months.

SUMMARY OF U.S. INTERNATIONAL TRANSACTIONS
(Billions of dollars, not seasonally adjusted except as noted)

	1995	1996	1996	1997				
			Q4	Q1	Q2	Q3	Sep	Oct
Official capital								
1. Change in foreign official reserve assets in U.S. (increase, +)	110.0	127.4	39.2	27.5	-6.0	22.9	10.3	-5.2
a. G-10 countries	33.1	36.7	3.4	7.5	4.6	2.0	1.8	-1.8
b. OPEC countries	4.3	15.3	5.5	7.0	2.5	3.6	-1.1	-3.2
c. All other countries	72.6	75.4	30.4	12.9	-13.1	17.2	9.6	-.2
2. Change in U.S. official reserve assets (decrease, +)	-9.7	6.7	-.3	4.5	-.2	-.7	-.1	-.1
Private capital								
Banks								
3. Change in net foreign positions of banking offices in the U.S.[1]	-30.9	-50.0	-7.8	-26.4	15.4	-4.2	-6.8	-10.8
Securities[2]								
4. Foreign net purchases of U.S. securities (+)	190.8	301.7	112.5	84.0	97.3	99.5	26.1	46.9
a. Treasury securities[3]	99.9	167.0	78.5	44.3	45.3	38.6	13.6	30.9
b. Corporate and other bonds[4]	82.6	122.6	32.4	29.0	29.9	36.9	7.3	12.9
c. Corporate stocks	8.2	12.1	1.5	10.7	22.1	24.0	5.2	3.1
5. U.S. net purchases (-) of foreign securities	-98.7	-105.9	-30.4	-17.1	-21.9	-38.6	-7.7	-3.1
a. Bonds	-48.4	-48.8	-19.9	-5.3	-8.6	-23.5	-7.8	-.8
b. Stocks	-50.3	-57.1	-10.5	-11.8	-13.3	-15.1	*	-2.3
Other flows (quarterly data, s.a.)								
6. U.S. direct investment (-) abroad	-86.7	-87.8	-30.9	-26.4	-36.7	-24.7	n.a	n.a
7. Foreign direct investment in U.S.	67.5	77.0	17.7	30.6	26.6	21.1	n.a	n.a
8. Foreign holdings of U.S. currency	12.3	17.3	7.8	3.5	4.8	6.6	n.a	n.a
9. Other (inflow, +)[5]	-10.6	-91.3	-67.6	-25.9	-27.2	-13.9	n.a	n.a
U.S. current account balance (s.a.)	-129.1	-148.2	-36.9	-40.0	-37.9	-42.2	n.a	n.a
Statistical discrepancy (s.a.)	-14.9	-46.9	-3.3	-14.3	-14.2	-25.8	n.a	n.a

Note. The sum of official capital, private capital, the current account balance, and the statistical discrepancy is zero. Details may not sum to totals because of rounding.

1. Changes in dollar-denominated positions of all depository institutions and bank holding companies plus certain transactions between broker-dealers and unaffiliated foreigners (particularly borrowing and lending under repurchase agreements). Includes changes in custody liabilities other than U.S. Treasury bills.

2. Includes commissions on securities transactions and therefore does not match exactly the data on U.S. international transactions published by the Department of Commerce.

3. Includes Treasury bills.

4. Includes U.S. goverment agency bonds.

5. Transactions by nonbanking concerns and other banking and official transactions not shown elsewhere plus amounts resulting from adjustments made by the Department of Commerce and revisions in lines 1 through 5 since publication of the quarterly data in the Survey of Current Business.

n.a. Not available. * Less than $50 million.

U.S. CURRENT ACCOUNT
(Billions of dollars, seasonally adjusted annual rates)

	Goods & services balance	Investment income, net	Transfers, net	Current acct balance
Years				
1995	-101.9	6.8	-34.0	-129.1
1996	-111.0	2.8	-40.0	-148.2
Quarters				
1995-1	-113.2	8.2	-33.8	-138.8
2	-123.2	12.9	-32.5	-142.8
3	-95.5	-1.6	-35.4	-132.5
4	-75.5	7.8	-34.5	-102.2
1996-1	-98.2	8.2	-41.6	-131.5
2	-111.1	3.5	-34.8	-142.3
3	-130.1	-5.5	-35.8	-171.3
4	-104.8	5.0	-47.7	-147.5
1997-1	-117.2	-8.0	-34.7	-159.9
2	-102.6	-13.0	-35.8	-151.4
3	-118.5	-13.3	-36.8	-168.6
Memo:				
$ Change				
1997:				
Q1-Q4	-12.4	-13.0	13.0	-12.4
Q2-Q1	14.6	-5.0	-1.1	8.5
Q3-Q2	-15.9	-0.3	-1.0	-17.2

Source. U.S. Department of Commerce, Bureau of Economic Analysis.

Foreign official assets in the United States (line 1) declined in October. In Asia, holdings of China and Hong Kong increased, but holdings of Taiwan, Singapore, Korea, and Malaysia declined. In Latin America there were substantial declines in holdings of Brazil and Mexico. Preliminary data from FRBNY indicate a sharp decline in Russian holdings in November.

Data recently released by the Department of Commerce indicate that foreign direct investment in the United States (line 7) slipped somewhat in the third quarter from the very strong pace of the first half. U.S. direct investment abroad (line 6) also slipped from the very high second-quarter level; the large intercompany outflows to finance company affiliates in the United Kingdom in the second quarter were reversed in part in the third quarter. Both inflows and outflows of direct investment continue to be swelled by numerous mergers and acquisitions.

INTERNATIONAL BANKING DATA[1]
(Billions of dollars)

	1994	1995	1996		1997			
	Dec.	Dec.	Sep.	Dec.	Mar.	Jun.	Sep.	Oct.
1. Net claims of U.S. banking offices (excluding IBFs) on own foreign offices and IBFs	-224.0	-260.0	-247.4	-231.2	-220.4	-225.7	-211.6	-189.3
a. U.S.-chartered banks	-70.1	-86.1	-73.6	-66.4	-72.5	-79.9	-77.9	-69.7
b. Foreign-chartered banks	-153.9	-173.9	-173.8	-164.8	-147.9	-146.0	-133.7	-119.6
2. Credit extended to U.S. nonbank residents								
a. By foreign branches of U.S. banks	23.1	26.5	29.2	31.9	32.9	33.4	34.0	34.1
b. By Caribbean offices of foreign-chartered banks	78.4	86.3	83.4	79.4	82.7	74.8	84.7	n.a
3. Eurodollar holdings of U.S. nonbank residents								
a. At all U.S.-chartered banks and foreign- chartered banks in Canada and the United Kingdom	86.3	94.6	103.4	119.5	128.1	134.0	139.9	138.7
b. At the Caribbean offices of foreign-chartered banks	86.0	92.3	109.4	122.2	135.5	130.6	130.3	n.a
MEMO: Data as recorded in the U.S. international transactions accounts								
4. Credit extended to U.S. nonbank residents	178.1	212.8	244.1	239.0	252.9	244.7	252.3	n.a.
5. Eurodeposits of U.S. nonbank residents	242.0	275.8	314.2	336.7	367.5	371.2	387.1	n.a.

1. Data on lines 1 through 3 are from Federal Reserve sources and sometimes differ in timing from the banking data incorporated in the U.S. international transactions accounts.
Lines 1a, 1b, and 2a are averages of daily data reported on the FR 2950 and FR2951.
Lines 2b and 3b are end-of-period data reported quarterly on the FFIEC 002s.
Line 3a is an average of daily data (FR 2050) supplemented by the FR 2502 and end-of-quarter data supplied by the Bank of Canada and the Bank of England. There is a break in the series in April 1994.
Lines 4 and 5 are end-of-period data estimated by BEA on the basis of data provided by the BIS, the Bank of England, and the FR 2502 and FFIEC 002s. They include some foreign-currency denominated deposits and loans. Source: SCB

Commerce Department data also indicate that the Eurodollar deposits of U.S. nonbanks continued to increase in the third quarter(line 5 on the International Banking Data Table). Credit extended to U.S. nonbanks from banks outside the United States also grew in the third quarter (line 4). Overall, recorded credits in the U.S. international transactions accounts continued to exceed recorded debits, resulting in a very large negative statistical discrepancy.

Foreign Exchange and International Asset Markets

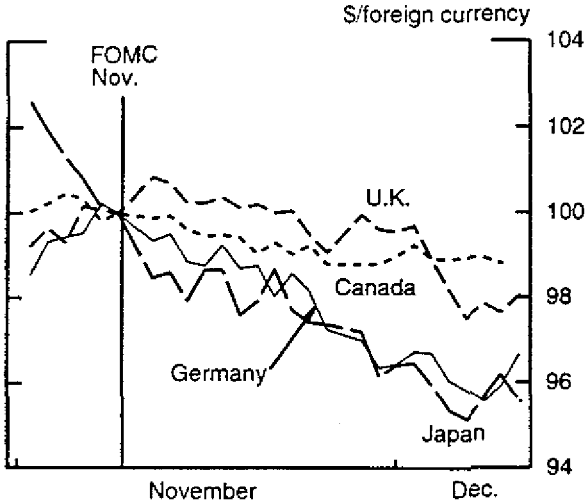
Since the November FOMC meeting, the dollar has strengthened 4 percent against the yen. The weakness of the yen vis-à-vis the dollar is generally attributed to concerns over financial fragility, the slow pace of economic activity, monetary easing by the Bank of Japan, and competitive pressures from other Asian economies. Japanese long-term bond yields have remained close to their historically low levels. The rise of the Japanese 3-month rate by 24 basis points reflects the emergence of a "Japan premium," an increased funding cost of Japanese banks, caused by heightened credit quality concerns as well as by end-of-year "window-dressing" efforts by non-Japanese banks to reduce their reported exposure to Japanese banks. Japanese share prices rose 2-1/2 percent on balance during the intermeeting period while undergoing sharp fluctuations, reflecting ongoing uncertainty over the manner in which the government will commit public funds to support the banking system.

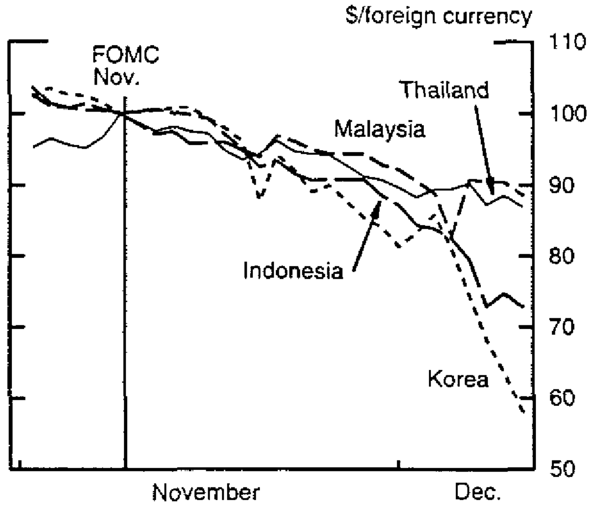
The Korean won, which had begun to depreciate earlier in the fall, accelerated its decline

. Immediately following the announcement of the IMF-led stabilization package the won gained 5 percent against the dollar, but depreciated rapidly thereafter on market concerns that the IMF package, even if implemented as announced, will fail to restore market confidence; on balance, the won depreciated 42 percent against the dollar through December 11. Korean share prices fell 28 percent over the same time period.

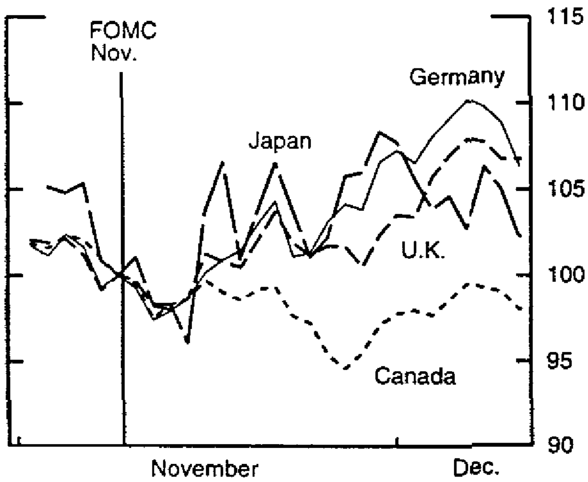
The currencies of the other East Asian emerging economies--the main exceptions being China and Hong Kong--also depreciated

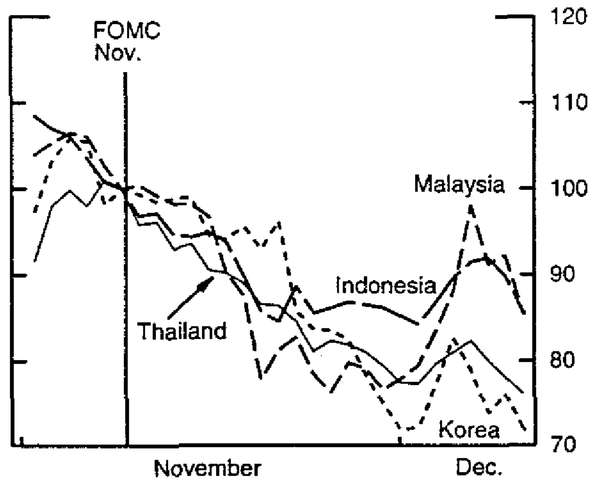
Exchange Rates
(Daily Indices, Nov. 10, 1997 = 100)





Stock Market Indices
(Daily Indices, Nov. 10, 1997 = 100)





Interest Rates in Major Industrial Countries

	Three-month rates			Ten-year bond yields		
	Nov. 10	Dec. 11	Change	Nov. 10	Dec.11	Change
Germany	3.65	3.70	0.05	5.61	5.33	-0.28
Japan	0.51	0.75	0.24	1.72	1.68	-0.04
United Kingdom	7.50	7.66	0.16	6.57	6.32	-0.25
Canada	4.03	4.33	0.30	5.54	5.73	0.19
France	3.55	3.57	0.02	5.64	5.33	-0.31
Italy	6.69	6.13	-0.56	6.16	5.72	-0.44
Belgium	3.79	3.58	-0.21	5.74	5.46	-0.28
Netherlands	3.66	3.67	0.01	5.60	5.30	-0.30
Switzerland	1.94	1.63	-0.31	3.51	3.25	-0.26
Sweden	4.48	4.73	0.25	6.41	6.11	-0.30
Weighted-average foreign	3.94	3.97	0.03	5.20	4.98	-0.22
United States	5.70	5.81[p]	0.11	5.91	5.81[p]	-0.10

Note. Change is in percentage points. [p] Preliminary.

against the dollar.

. The Thai baht declined further after the debt ratings of several Thai financial institutions were downgraded; on balance, the baht declined 13 percent. The Malaysian ringgit fell 12 percent, while the Philippine peso fell 6-1/2 percent. The Singapore dollar and Taiwan dollar participated to a lesser degree in the waves of depreciations; these two currencies declined 2-1/2 and 3-3/4 percent against the dollar, respectively.

Equity prices in most East Asian emerging economies continued to decline on reports of mounting economic difficulties. Thailand's stock market fell 24 percent in the intermeeting period, and Indonesian share prices fell 14 percent. Malaysia's stock market, which fell sharply earlier in the intermeeting period, reacted positively to new, austere budget measures proposed by the government in late November, rising 12 percent on balance since December 1. The Philippine stock market rose 1-1/4 percent on balance.

The dollar strengthened 3-1/2 percent against the mark. The mark's depreciation occurred amid data releases that indicate that German inflation continues to be benign and output growth moderate. In addition, statements by Bundesbank officials that they see no immediate need to raise interest rates to contain inflation and comments by several European central bank officials that European-wide interest rates will converge closer to the low end of the current spectrum of European interest rates also weighed on the mark. German and French bond yields fell about 30 basis points during the intermeeting period; corresponding short-term interest rates were largely unchanged. Italian short-term rates fell 56 basis points and long-term rates fell 44 basis points, reflecting the continued movement of Italian rates towards German and French rates. The Swedish central bank announced on December 11 that it would raise its repo rate by 25 basis points to 4.35 percent; the Riksbank stated that this policy measure was taken in order to help meet its 1998 inflation targets.

The U.S. dollar strengthened 1-1/4 percent against the Canadian dollar. The Canadian currency's weakness was attributed by some market analysts to falling commodity prices following the sharp decline of Asian growth. The Bank of Canada raised its Bank Rate by 25 basis points on November 25 to offset the stimulative effect of the depreciating Canadian dollar. The Canadian long-term bond yield increased by 19 basis points and the Canadian 3-month interest rate rose by 30 basis points, in step with the increase in the overnight policy rate set by the Bank of Canada. The dollar strengthened 2 percent against sterling, supported by a narrowing of the spread between U.K. and U.S. long-term interest rates.

Share prices in the industrialized countries, with the exception of Canada, are up since the November FOMC meeting and have recovered most of the losses sustained in late October and early November. Equity prices in Germany and the United Kingdom rose 7 and 5 percent, respectively, during the intermeeting period. The comparative weakness of the Canadian stock market, which fell almost 2 percent on balance, is being attributed to the effects of declining world market prices of primary commodities and gold on the profitability of a large number of Canadian companies.

The exchange value of the Mexican peso, which had fallen sharply against the dollar in late October and early November, has risen 3/4 percent since the last FOMC meeting. The peso's rebound may be attributed to rising market confidence in the ability of Mexico to weather the financial crises originating in Asia. Yield spreads on Latin American Brady bonds, which had increased in October, fell by 140 and 210 basis points in the intermeeting period. The stock markets of Brazil, Mexico, and Argentina rose between 5 and 10 percent.

The Czech koruna fell 6 percent against the dollar on the fallout of a political scandal and the subsequent resignation of the entire Czech cabinet towards the end of November. The Russian ruble fell 3/4 percent vis-à-vis the dollar.

The price of gold has declined 8 percent since the November FOMC to $284 per fine ounce, as markets perceived a continued trend towards a lower demand for monetary gold by the world's central banks.

. The Desk did not intervene in the foreign exchange market during the period.

Developments in Foreign Industrial Countries

Real GDP growth in the foreign G-7 countries averaged about 4 percent on an export-weighted basis in the third quarter, and preliminary indicators for the fourth quarter suggest continued above-trend growth in most countries. The pace of expansion remains particularly robust in Canada and the United Kingdom, fueled largely by strong domestic demand growth. Both the German and French economies also continued to expand at healthy rates in the third quarter. However, Italian growth has slowed in the second half of the year, while the Japanese economy has rebounded only modestly following last April's consumption tax increase. The impact of the crisis in southeast Asia, which is expected to be much more severe in Japan than in the other countries, has not yet become fully apparent in current indicators.

Unemployment generally remains high, and year-over-year consumer price inflation is currently below 2 percent in Canada and the major continental European countries. Although the consumption tax increase and some other temporary factors have recently pushed measured inflation in Japan to around 2 percent, the underlying rate remains low there as well. In contrast, recent evidence suggests that inflationary pressure is continuing to build in the United Kingdom as labor markets tighten.

Individual country notes. In **Japan**, third-quarter GDP expanded at a 3.1 percent rate, registering only a modest rebound from the second quarter's double-digit decline. Private consumption retraced about a third of its second-quarter drop, led by an increase in new car sales. Private non-residential investment grew at a 6½ rate, offsetting a second-quarter decline of identical magnitude. Residential investment, however, plunged by 36 percent, reaching its lowest level since the first quarter of 1987. Government consumption and public investment jointly contributed ¾ of a percentage point to growth, partially reversing declines registered in recent quarters. Net exports made a negative contribution to growth as exports fell a bit from their very high se:ond-quarter levels.

JAPANESE REAL GDP
(Percent change from previous period, SAAR) [1]

	1995	1996	1996	1997		
			Q4	Q1	Q2	Q3
GDP	2.4	3.4	4.3	8.3	-10.6	3.1
Total Domestic Demand	3.8	3.3	2.9	7.8	-14.3	3.7
Consumption	2.6	2.4	3.8	16.8	-19.5	6.5
Investment	6.3	6.0	2.3	-4.2	-10.1	-1.4
Government Consumption	2.9	1.8	4.1	-3.7	-3.7	2.9
Inventories (contribution)	0.1	-0.2	-0.5	-0.1	1.1	0.0
Exports	3.7	8.0	20.8	5.7	25.1	-5.0
Imports	17.3	7.0	8.1	1.8	-8.7	-1.8
Net Exports (contribution)	-1.3	0.2	1.5	0.5	3.8	-0.5

1. Annual changes are Q4/Q4.

Economic indicators for the fourth quarter suggest a continuation of the economy's lackluster performance. Industrial production during October and new car registrations during October and November were essentially unchanged from their third-quarter levels, and labor market conditions appear to be deteriorating. Infl3tion, net of the effect of the tax increase, remains virtually nonexistent.

Import volumes in October increased slightly from third-quarter levels, but the volume of exports was up by 10 percent. However, the October data provided the first glimpse of the effects of the Asia crisis on Japanese trade, with exports to Thailand declining 20 percent from their year-earlier level. In addition, foreign orders for machinery fell sharply in October.

In mid-November, the Japanese government released a package of 120 economic stimulus measures, including proposals for further deregulation, plans to improve the liquidity of the real estate market and the efficiency of land use, and measures designed to stimulate private investment. However, the government's package

JAPANESE ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1997						
	Q1	Q2	Q3	Aug	Sep	Oct	Nov
Industrial Production	2.5	-0.1	-0.3	-3.0	2.4	-0.4	n.a.
Housing Starts	-10.9	-5.2	-10.6	5.6	1.7	2.6	n.a.
Machinery Orders	-3.1	6.0	1.3	-2.9	1.1	-9.7	n.a.
New Car Registrations	2.3	-23.9	4.8	-4.9	10.8	-1.4	-8.5
Unemployment Rate (%)	3.3	3.4	3.4	3.4	3.4	3.5	n.a.
Job Offers Ratio[1]	0.74	0.73	0.72	0.72	0.71	0.70	n.a.
Business Sentiment[2]	2	7	3	...	...	...	...
CPI (Tokyo area)[3]	0.0	1.5	1.7	1.6	2.2	2.4	2.0
Wholesale Prices[3]	1.4	2.6	2.0	2.1	2.0	1.6	1.5

1. Level of indicator.
2. Percent of large manufacturing firms having a favorable view of business conditions less those with an unfavorable view (Tankan survey).
3. Percent change from previous year, NSA.

largely reflected two previously released LDP packages, and did not include any direct fiscal stimulus measures.

In recent weeks, two large Japanese financial institutions have failed. On November 17, the Japanese authorities announced the closure of Hokkaido Takushoku Bank (HTB), one of the twenty-five largest Japanese banks with assets of ¥9 trillion (about $72 billion). The majority of HTB's operations will be assumed by Hokuyo Bank, a second-tier regional bank in Hokkaido. All of HTB's depositors will be protected, but its management will be forced to resign. On November 24, Yamaichi Securities, Japan's fourth-largest brokerage house, reported that it was voluntarily suspending operations. Yamaichi announced that its capital base, which was previously reported as ¥431 billion (about $3.4 billion) at end-September 1997, was being revised downward by ¥265 billion (about $2.1 billion), reflecting the acknowledgement of unrealized losses and a variety of other off-balance-sheet debt. The Bank of Japan has provided liquidity to both Hokkaido Takushoku Bank and Yamaichi Securities, as well as to the market as a whole, in an effort to minimize disruptions as these institutions conclude their business operations.

Real GDP in **Germany** rose at a 3.2 percent annual rate in the third quarter. The external sector continued to provide the primary impetus to growth, as exports rose at a double-digit rate for the second consecutive quarter. In contrast, private consumption declined sharply, retreating to its first-quarter level. Although the growth in total investment was modest, spending on machinery and equipment was up sharply. Inventory accumulation was sizable, but inventory figures are a residual in the national accounts and are subject to substantial revision.

GERMAN REAL GDP
(Percent change from previous period, SAAR) [1]

	1995	1996	1996	1997		
			Q4	Q1	Q2	Q3
GDP	0.7	2.1	0.9	1.2	4.1	3.2
Total Domestic Demand	0.5	1.3	1.4	1.1	0.9	0.4
Consumption	1.6	1.2	-1.4	-0.7	5.0	-4.2
Investment	-2.8	2.4	1.0	-8.3	1.2	1.7
Government Consumption	2.8	-0.1	-8.2	5.9	1.6	2.6
Inventories (contribution)	-0.4	0.1	3.7	2.2	-2.5	1.9
Exports	5.3	8.1	13.6	8.3	15.1	16.5
Imports	4.1	4.8	15.5	8.0	3.4	6.4
Net Exports (contribution)	0.3	0.8	-0.4	0.1	3.2	2.8

1. Annual changes are Q4/Q4.

Early indicators for the fourth quarter suggest that the economic expansion continued. Industrial production rose sharply in October following the declines registered in August and September. Manufacturing orders fell in October for a second consecutive month but remain at a high level following rapid gains over the two preceding quarters. The October decline was due primarily to a sharp drop in orders from foreign firms, while domestic orders showed a strong gain. Business confidence also dropped back a little in October but remains high. However, conditions in the labor market are still stagnant, with the all-German unemployment rate remaining at 11.8 percent in November. CPI inflation has fallen back recently to below 2 percent on a 12-month basis, following a slight acceleration during the summer.

GERMAN ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1997						
	Q1	Q2	Q3	Aug	Sep	Oct	Nov
Industrial Production	0.2	1.0	1.9	-4.6	-0.4	1.8	n.a.
Orders	1.1	3.9	2.5	1.4	-0.5	-0.8	n.a.
Unemployment Rate (%)	11.2	11.3	11.6	11.6	11.7	11.8	11.8
Western Germany	9.8	9.9	9.9	9.9	9.9	9.9	9.9
Eastern Germany	17.0	17.5	18.8	18.8	19.2	19.4	19.6
Capacity Utilization[1]	84.1	85.1	86.0	...	...	...	...
Business Climate[1,2]	1.3	6.7	16.0	16.0	19.0	17.0	n.a.
Consumer Prices[3]	1.7	1.6	1.9	2.1	1.9	1.8	1.9

1. Western Germany.
2. Percent of firms (in manufacturing, construction, wholesale, and retail) citing an improvement in business conditions (current and expected over the next six months) less those citing a deterioration in conditions.
3. Percent change from previous year.

In **France**, third-quarter real GDP increased at a 3.7 percent annual rate, following a 4.5 percent rate increase in the second quarter. Domestic demand growth more than accounted for the robust third-quarter expansion, as the contribution from net exports turned negative. Consumption growth picked up sharply from its sluggish pace earlier in the year, and investment growth increased as well, contrary to expectations. Given the imprecise nature of initial investment estimates and the variable consumption performance, it is still early to tell whether the economic expansion has become more broadly-based. Increased investment over the past two quarters, however, is consistent with recent strength in capital goods production, which business surveys and balance of trade data had earlier suggested were primarily export-oriented.

The limited information available so far for the fourth quarter suggests that economic activity is continuing to expand, although probably at a more moderate pace than in the third quarter. Consumption of manufactured products rebounded in October following

FRENCH REAL GDP
(Percent change from previous period, SAAR)[1]

	1995	1996	1996 Q4	1997 Q1	1997 Q2	1997 Q3
GDP	0.3	2.2	1.2	1.2	4.5	3.7
Total Domestic Demand	0.1	1.4	0.2	-1.6	1.9	5.2
Consumption	0.8	1.8	-2.0	0.8	0.4	4.5
Investment	0.1	-0.4	0.8	-5.1	2.0	7.0
Government Consumption	0.2	1.8	2.0	1.6	1.2	1.2
Inventories (contribution)	-0.4	0.0	0.8	-1.3	1.1	0.7
Exports	1.6	8.6	8.2	9.1	22.9	10.0
Imports	0.9	5.8	4.9	-0.4	14.3	15.6
Net Exports (contribution)	0.2	0.8	1.0	2.8	2.6	-1.4

1. Annual changes are Q4/Q4.

two months of declines to a level slightly above the third-quarter average, partly reflecting increased back-to-school allowances. However, business surveys in October-November continue to highlight strong foreign orders (which have not been affected to date by the crisis in emerging-Asia), and do not indicate a further acceleration in domestic demand. Also, investment expectations for 1997 have been revised down. The unemployment rate has remained at an historically high level of 12.5 percent all year, and inflation pressures remained subdued.

FRENCH ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1997 Q1	Q2	Q3	Aug	Sep	Oct	Nov
Consumption of Manufactured Products	0.9	-0.4	2.5	-1.9	-1.9	2.2	n.a.
Industrial Production	0.2	2.5	1.6	0.0	-1.0	n.a.	n.a.
Capacity Utilization	83.6	83.8	84.5	...	...	...	...
Unemployment Rate (%)	12.5	12.5	12.5	12.5	12.5	12.5	n.a.
Business Confidence[1]	10.3	8.3	14.5	...	18.0	16.0	18.0
Consumer Prices[2]	1.5	0.9	1.3	1.5	1.3	1.0	1.3

1. Percent balance of manufacturing firms citing an improvement in the outlook versus those citing a worsening; no August survey conducted.
2. Percent change from previous year.

Real GDP in the **United Kingdom** increased at a 3.6 percent annual rate in the third quarter. Consumer spending registered another quarter of strong growth, while the contribution of net exports turned positive again. Fixed investment declined, as the aircraft orders that gave rise to the upturn earlier in the year were not repeated; fixed investment excluding aircraft increased at about a 2 percent rate in the third quarter.

UNITED KINGDOM REAL GDP
(Percent change from previous period, SAAR) [1]

	1995	1996	1996	1997		
			Q4	Q1	Q2	Q3
GDP	2.0	2.9	4.3	3.4	4.0	3.6
Total Domestic Demand	1.1	3.0	4.5	3.0	5.9	2.5
Consumption	1.6	4.3	5.2	3.3	6.2	4.8
Investment	-1.6	3.7	10.5	2.0	8.2	-4.6
Government Consumption	1.3	2.4	1.5	-0.5	0.7	0.1
Inventories (contribution)	0.1	-0.7	-0.8	0.7	0.5	0.4
Net Exports (contribution)	0.9	-0.4	-0.3	0.8	-1.8	0.8
Non-oil GDP	1.9	2.8	4.5	3.7	4.0	4.0

1. Annual changes are Q4/Q4.

Preliminary indicators for the fourth quarter suggest that growth remains strong. The average volume of retail sales surged in October, more than offsetting a decline in September. Spending in September had been depressed by a number of special factors, including unusually low sales in the week leading up to the funeral of Princess Diana. Although business sentiment weakened somewhat in November, the Purchasing Managers Survey of manufacturers indicated that new domestic orders rose sharply, while export orders increased moderately.

Conditions in the labor market have continued to tighten. The official claimant unemployment rate was unchanged at 5.2 percent in October, but surveys suggest that skill shortages and recruitment difficulties have increased. Growth of nominal earnings remains moderate. Retail prices excluding mortgage interest payments rose

2.8 percent over the year to November, remaining above the government's inflation target of 2½ percent for underlying inflation. Producer input prices continued to decline in November, reflecting the strength of sterling.

UNITED KINGDOM ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1997						
	Q1	Q2	Q3	Aug	Sep	Oct	Nov
Industrial Production	0.1	0.7	1.2	-0.8	-0.1	-0.3	n.a.
Retail Sales	1.1	1.9	1.0	0.3	-1.9	2.9	n.a.
Unemployment Rate (%)	6.3	5.8	5.3	5.3	5.2	5.2	n.a.
Business Confidence[1]	18.3	17.7	18.0	16.0	17.0	20.0	9.0
Consumer Prices[2]	2.9	2.6	2.8	2.8	2.7	2.8	2.8
Producer Input Prices[3]	-7.1	-9.6	-8.4	-8.1	-8.3	-9.0	-8.3
Average Earnings[3]	4.6	4.3	4.4	4.5	4.3	n.a.	n.a.

1. Percent of firms expecting output to increase in the next four months minus those expecting output to decrease.
2. Retail prices excluding mortgage interest payments. Percent change from previous year.
3. Percent change from previous year.

In its November *Inflation Report*, the Bank of England noted that both output growth and inflation have turned out to be about ½ percentage point higher than in the central projection made for the August *Report*, reflecting a surprisingly muted effect of sterling's appreciation on net trade, while the impact of the higher exchange rate on the domestic price level has been restrained by rising profit margins. For the first time, the *Inflation Report* gave the Bank's projection for real GDP growth as well as inflation over the forecast period. The Bank's central projection is for growth to fall below 2 percent in 1998, but then to pick up somewhat in 1999. Inflation is projected to be around the government's target rate of 2½ percent. The Monetary Policy Committee decided not to reinstate the monitoring ranges for the M0 and M4 aggregates, which had lapsed in May when the Bank was granted operational independence, noting that velocity has behaved erratically recently.

In **Italy**, GDP rose at a preliminary 1.6 percent rate in the third quarter. Although actual data on the breakdown of expenditures are not yet available, the Italian statistical agency indicated that final domestic demand growth was strong, with both household consumption and business investment contributing positively. Inventory accumulation, which contributed over 6 percentage points to second-quarter growth, slowed in the third quarter. Preliminary data also indicated that the pass-through effects of the highly successful auto-tax incentives continued in the third quarter.

Fourth-quarter indicators are very limited. Consumer confidence in October and November was slightly below its third-quarter average, but remained significantly higher than its level in the second quarter. Business sentiment also declined in October, reaching its lowest level since June.

Italian inflation remains low. In November, consumer prices rose 1.6 percent (yr/yr), the same rate registered in the previous month. Although the pass-through effects of the rise in VAT last month put upward pressure on consumer prices in November, they were to a large extent offset by a moderation in food and energy prices.

ITALIAN ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1997						
	Q1	Q2	Q3	Aug	Sep	Oct	Nov
Industrial Production	1.4	2.2	0.5	1.0	-0.7	n.a.	n.a.
Cap. Utilization (%)	76.2	77.7	77.7	...	...	...	...
Unemployment Rate (%)	12.2	12.4	12.1	...	...	...	...
Consumer Confidence[1]	109.2	108.8	117.2	117.8	119.7	116.1	116.7
Bus. Sentiment[2] (%)	20.0	13.7	18.0	21.0	18.0	12.0	n.a.
Consumer Prices[3]	2.4	1.6	1.6	1.6	1.5	1.6	1.6
Wholesale Prices[3]	0.6	-0.4	0.4	0.9	0.5	n.a.	n.a.

1. Level of index, NSA.
2. Percent of manufacturing firms having a favorable view of business conditions minus those with an unfavorable outlook.
3. Percent change from previous year.

On November 21, the Senate (the upper house) approved the government's 1998 budget proposal, which includes a total of $15 billion equivalent (or about 1½ percent of GDP) in deficit cutting measures. Roughly $3 billion of the planned reductions arise from lower welfare spending. Under Italian law, the budget proposal, which is currently under consideration in the lower house of the parliament, is required to be approved by the end of December.

The **Canadian** economy continues to grow at a robust rate. Real GDP at factor cost increased at a 4.8 percent rate in the third quarter, with home-building and wholesale sales of machinery and equipment showing particular strength. Most of the third-quarter gain came in July, however, with monthly output growth slowing in the August-September period. Employment growth resumed in November, after a pause in September-October. The unemployment rate moved back down to 9.0 percent in November, reversing an uptick in October, and would have moved even lower if not for a strong increase in the labor force. September retail sales and October housing starts also showed continued strength. Consumer price inflation slowed a bit in October to 1.5 percent on a twelve-month basis, showing little evidence of immediate price pressures despite the strong economy.

Recent data on trade and the current account provide perhaps the most significant indication of strong Canadian domestic demand. The current account deficit widened more sharply than expected in the third quarter, to $4.6 billion, from $2.8 billion in the second quarter. The increase in the deficit was largely due to a decline in the surplus on trade in goods, as strong growth in domestic demand led to a surge in imports, especially of equipment and machinery. Monthly trade data showed a steady shrinking of the trade surplus month-by-month during the third quarter, as imports grew at a rapid clip.

The Bank of Canada increased its key Bank Rate ¼ percentage point, to 4 percent, on November 25, the third such increase this year. The Bank indicated that it was responding to the recent weakness in the Canadian dollar, related to the impact of the Asian crisis on the prices of commodities produced intensively in Canada. As measured by the Bank's monetary conditions index, currency weakness had reversed all of the monetary tightening put in place with the rate hike on October 1; the Bank indicated that such an easing of monetary conditions was not appropriate at this time.

CANADIAN ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1997						
	Q1	Q2	Q3	Aug	Sep	Oct	Nov.
GDP at Factor Cost	0.9	1.2	1.2	0.0	0.2	n.a.	n.a.
Industrial Production	0.9	1.7	1.7	-0.4	-0.3	n.a.	n.a.
Manufacturing Survey: Shipments	2.9	0.9	2.4	-2.7	-0.3	n.a.	n.a.
New Orders	4.5	1.4	1.9	-2.9	0.2	n.a.	n.a.
Retail Sales	2.1	1.7	1.7	0.3	0.3	n.a.	n.a.
Housing Starts	19.9	-6.3	2.4	1.6	-1.7	3.5	n.a.
Employment	0.3	0.9	0.8	0.4	0.1	-0.1	0.2
Unemployment Rate (%)	9.6	9.4	9.0	9.0	9.0	9.1	9.0
Consumer Prices[1]	2.1	1.6	1.7	1.8	1.6	1.5	n.a.
Consumer Attitudes[2]	108.0	116.7	119.3	...	...	...	...
Business Confidence[3]	160.1	165.0	164.9	...	...	...	...

1. Percent change from year earlier.
2. Level of index, 1991 = 100.
3. Level of index, 1977 = 100.

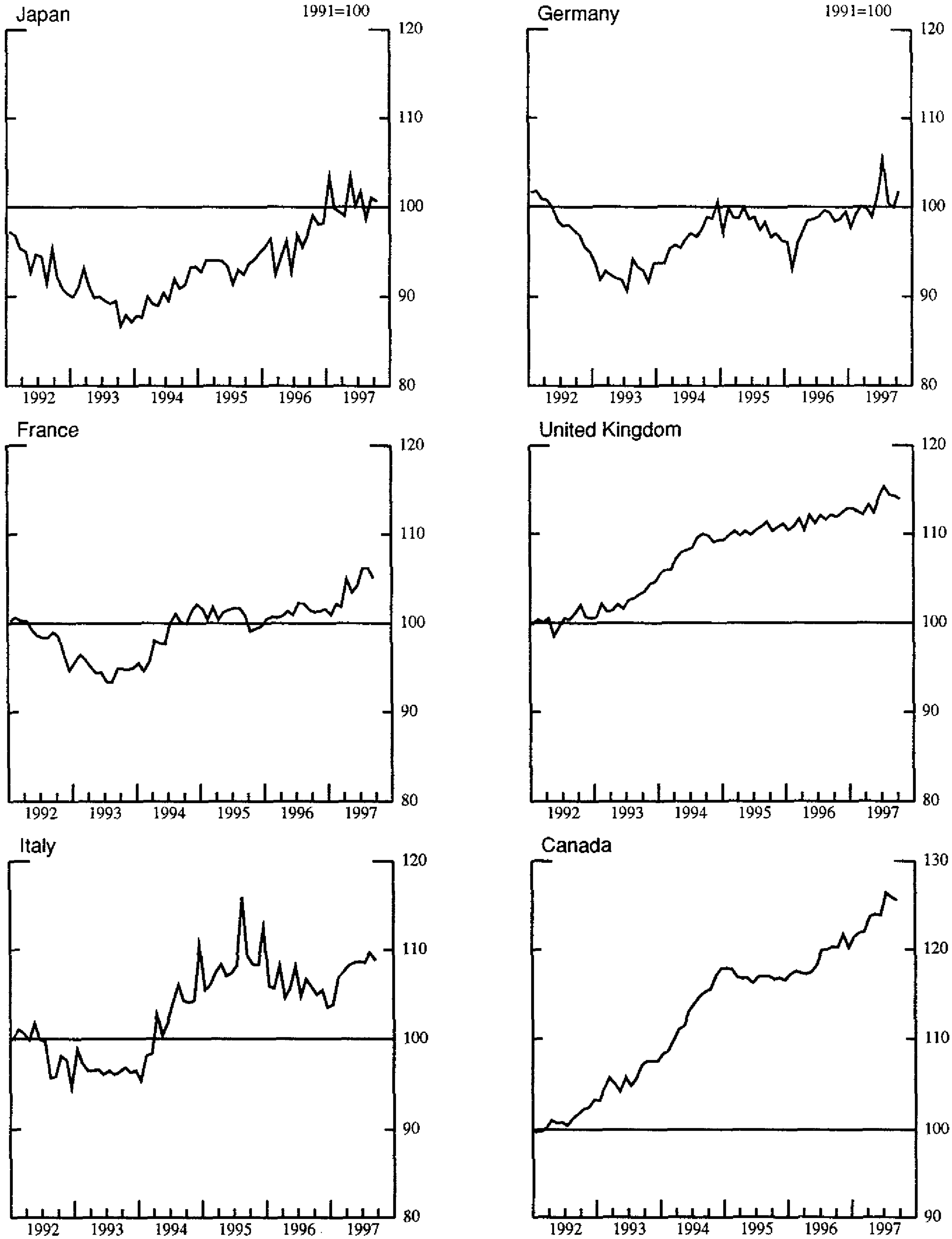
EXTERNAL BALANCES
(Billions of U.S. dollars, seasonally adjusted)

	1996	1997						
		Q1	Q2	Q3	Jul	Aug	Sep	Oct.
Japan: trade	61.4	12.9	23.3	21.7	6.3	9.1	6.2	10.2
current account	65.9	15.4	26.4	24.9	8.1	10.2	6.6	11.1
Germany: trade[1]	65.4	14.7	19.3	20.2	7.2	4.7	8.3	n.a.
current account[1]	-13.1	-5.8	2.9	-1.9	-0.5	-3.0	1.6	n.a.
France: trade	17.0	5.5	8.6	8.4	3.5	1.7	3.2	n.a.
current account	21.9	8.9	11.5	n.a.	4.1	1.5	n.a.	n.a.
U.K.: trade	-19.6	-4.0	-4.2	-4.1	-1.1	-1.0	-2.0	n.a.
current account	-0.60	2.2	1.5	n.a.	...	...	...	...
Italy: trade	44.5	8.7	7.9	n.a.	6.2	2.8	n.a.	n.a.
current account[1]	41.1	8.8	7.0	n.a.	8.2	2.6	n.a.	n.a.
Canada: trade	30.0	6.0	4.2	2.7	1.2	0.9	0.6	n.a.
current account	2.8	-0.7	-2.8	-4.6	...	...	...	...

1. Not seasonally adjusted.
... Data not available on a monthly basis.

DECEMBER 11, 1997

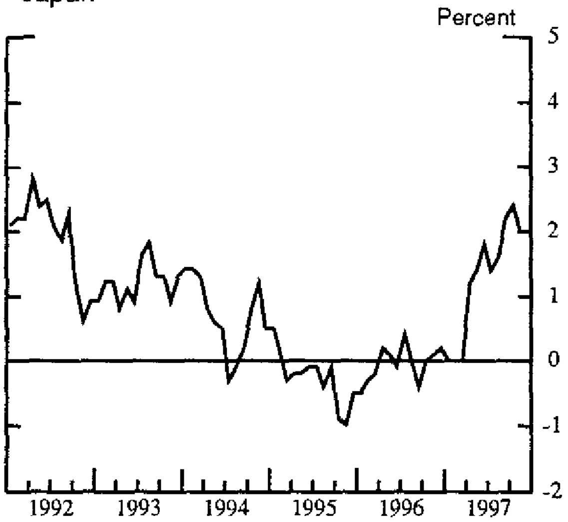
Industrial Production in Selected Industrial Countries



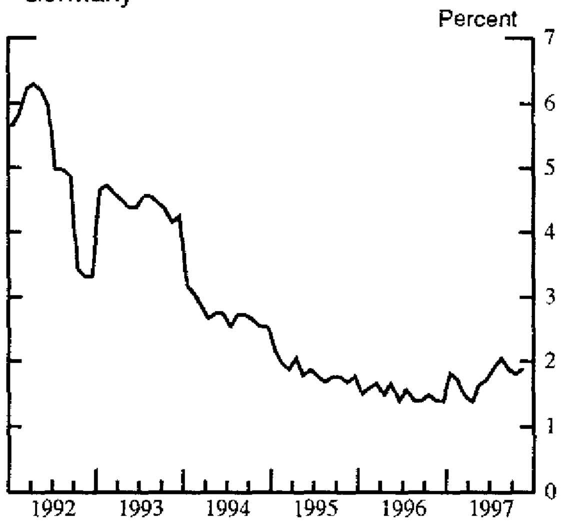
DECEMBER 11, 1997

Consumer Price Inflation in Selected Industrial Countries
(12-month change)

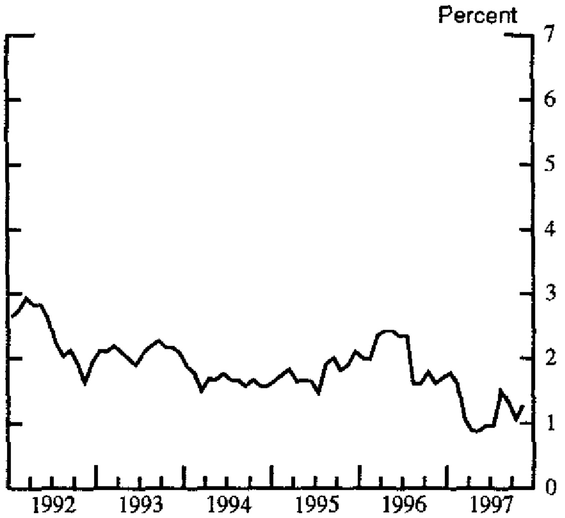
Japan



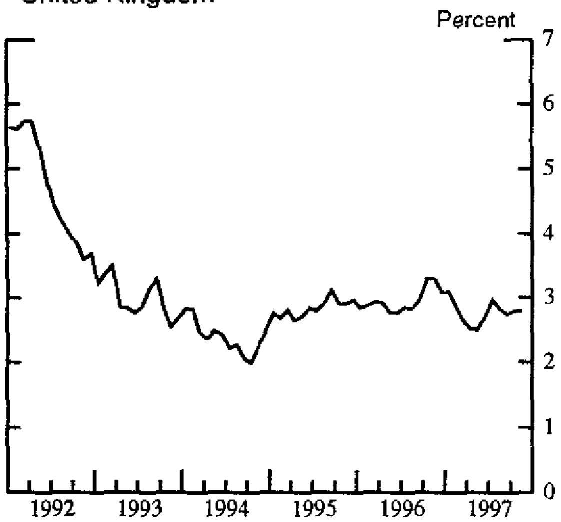
Germany



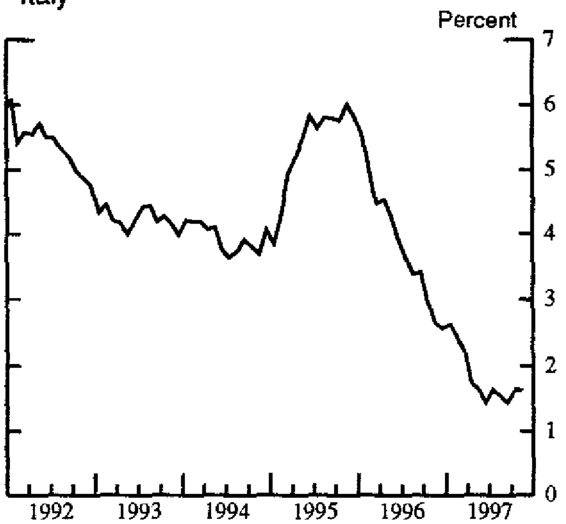
France



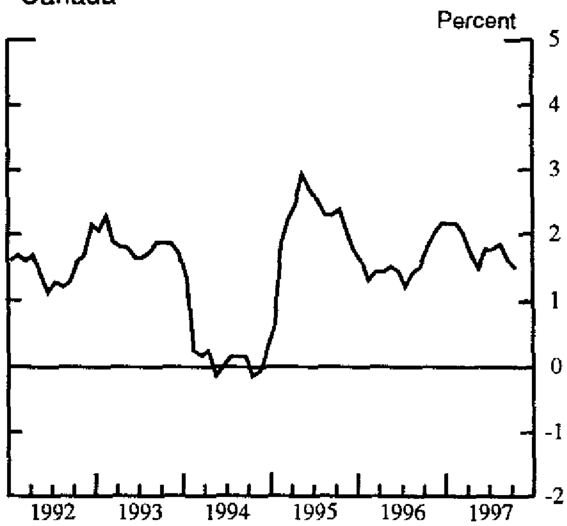
United Kingdom



Italy



Canada



Economic Situation in Other Countries

Financial turmoil has shown little signs of abating in the ASEAN region. In Korea, a major financial crisis has erupted, prompting the government to seek international financial assistance. By early December, downward pressures on currencies had abated in Hong Kong, Brazil, and Argentina, but renewed pressures emerged in the wake of the deterioration of conditions in Korea.

The financial turmoil in the five major ASEAN countries has led to a significant slowdown in growth in the region. In contrast, growth has remained strong in Korea, whose troubles reached crisis proportions only recently, and in Taiwan and China. Growth performance was also good in major Latin American countries in the third quarter. External imbalances in the ASEAN region have narrowed as a result of the fall in domestic demand and currency depreciations.

ASEAN and individual country notes. In **Korea**, a serious financial crisis has erupted following several months of mounting concern about the health of Korean banks. Most of Korea's major banks have heavy exposure to several large industrial conglomerates that failed earlier in the year. In October and November, increased concern about bank solvency put the won under strong downward pressures. By December 2, the won was 25 percent below its level on October 30. Over that period, the stock market fell by 25 percent to its lowest level since May 1987, and the yield on 3 year won-denominated corporate bonds rose over 500 basis points.

On December 3, Korea and the IMF reached agreement on an IMF-led assistance package that will total roughly $57 billion. The IMF will provide $21 billion in the form of a three-year standby arrangement with the first $10 billion to be distributed in three tranches over a five-week period. This will be supplemented by $10 billion from the World Bank and $4 billion from the Asian Development Bank. The United States, Japan, and other major industrial countries have also agreed to provide over $20 billion collectively in bilateral assistance. The assistance would be provided only as a backup to the support from the multilateral agencies and could only be drawn upon subject to stringent conditions. The U.S. support would come from the U.S. Treasury's Exchange Stabilization Fund.

The IMF plan requires, first, that Korea rapidly restructure its troubled banking sector. Weak banks will be merged with healthier ones, and some insolvent banks will be closed. Second, it requires a very substantial and nearly immediate opening of the capital account. Foreign investors will be allowed to purchase a majority stake in Korean companies and buy Korean bonds without restriction. Third, Korea must pass legislation that grants autonomy to the Bank of Korea (BOK) and makes price stability its primary objective. Fourth, the BOK is required to maintain a tight monetary policy stance.

Financial markets have been volatile since the announcement of the program. By December 11, the won was 34 percent below its December 2 close, while the stock price index was basically unchanged after a rollercoaster ride. Korea will hold its presidential election on December 18, but none of the three candidates has articulated a plan for resolving the current crisis.

Korea's crisis comes against the backdrop of a modest pickup in Korea's economic growth and improvement in its trade balance. The trade balance improvement has reflected in part a depreciation of the Korean won against the U.S. dollar. (The won declined by about 16 percent between March 1996 and mid-October 1997, prior to its precipitous drop that began in late October.) Inflation has remained quite low.

KOREAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1996	1997			1997		
		Q1	Q2	Q3	Sep	Oct	Nov
Real GDP	6.8	5.3	6.3	6.3	...	...	...
Industrial Production	8.4	7.0	9.7	8.9	10.1	12.2	n.a.
Consumer Prices	5.0	4.7	4.0	4.0	4.2	4.3	4.3
Trade Balance[1]	-15.3	-5.4	-0.8	0.1	0.3	-0.0	n.a.
Current Account[1]	-23.7	-7.9	-3.0	-2.2	-0.5	-0.7	n.a.

1. Billions of U.S. dollars, NSA

The turmoil in financial markets in the **ASEAN** region has shown little sign of abating. Since the last Greenbook, the currencies of Indonesia, Malaysia, the Philippines, Singapore, and Thailand have further depreciated against the dollar and stock indices have continued to decline. In most countries, interest rates have remained at elevated levels. In Singapore, where interest rate increases were very modest so far, two of the "Big Four" banks raised their prime rates last week.

The substantial increases in interest rates since July appear to be slowing domestic demand growth considerably in the ASEAN region. Malaysia's real GDP growth in the third quarter was under 4 percent (s.a.a.r), its slowest pace in four years. In the Philippines, real GDP grew by just over 2 percent (s.a.a.r) in the third quarter, a sharp slowdown from the pace in the first half of the year. Singapore, however, posted robust growth in the third quarter, boosted by strong recovery in global electronics demand. In Thailand, industrial production contracted sharply in the third quarter.

ASEAN ECONOMIC INDICATORS: GROWTH

	1996	1997			1997		
		Q1	Q2	Q3	Sep	Oct	Nov
Real GDP, s.a.a.r.							
Indonesia	7.8	n.a.	n.a.	n.a.	...	...	...
Malaysia	8.6	6.9	9.1	3.9	...	...	...
Philippines	5.7	6.0	10.3	2.2	...	...	...
Singapore	6.7	4.8	15.6	6.5	...	...	...
Thailand	6.4	n.a.	n.a.	n.a.	...	...	...
Industrial Production[1]							
Malaysia	11.0	11.6	11.8	9.3	7.5	n.a.	n.a.
Thailand	7.2	6.0	5.8	-2.7	-6.7	n.a.	n.a.

1. Year-over-Year

Inflation has picked up substantially in some economies in the region, driven in large part by the substantial depreciations of their currencies. In Indonesia, inflation rose to 10 percent in November (year-over-year); a long drought has exacerbated the inflationary pressure. Inflation has so far remained at low levels in Malaysia and Singapore.

ASEAN ECONOMIC INDICATORS: INFLATION
(Percent change from year earlier)

	1996	1997			1997		
		Q1	Q2	Q3	Sep	Oct	Nov
Consumer Prices							
Indonesia	8.0	5.2	4.9	6.0	6.9	8.5	9.9
Malaysia	3.5	3.2	2.5	2.3	2.3	2.7	n.a.
Philippines	8.4	4.7	4.5	4.9	5.3	5.7	6.5
Singapore	1.4	1.6	1.8	2.3	2.5	2.5	n.a.
Thailand	5.8	4.4	4.4	6.2	7.2	7.6	7.6

Trade balances improved significantly in economies in the ASEAN region as a result of the substantial real depreciation of their currencies, the slowdown in their growth, and strong growth in industrialized countries (except Japan). Thailand reported balanced trade in September, in contrast to a decade of trade deficits.

ASEAN ECONOMIC INDICATORS: TRADE BALANCE

	1996	1997			1997		
		Q1	Q2	Q3	Aug	Sep	Oct
Trade Balance[1]							
Indonesia	6.9	1.7	2.4	3.7	1.5	1.2	n.a.
Malaysia	-0.2	0.8	-1.9	0.5	0.4	0.4	0.0
Philippines	-11.4	-2.9	-2.6	-2.6	-1.0	-0.5	n.a.
Singapore	2.3	-0.0	0.9	0.2	-0.3	0.7	0.3
Thailand	-9.5	-3.2	-3.2	-1.4	-0.7	0.0	n.a.

1. Billions of U.S. dollars

The response of policymakers to the regional financial crisis has been mixed. Progress on Indonesia's IMF program--which got off to a good start with the closure of some banks and with intervention boosting the rupiah--appears to have stalled. The Philippines is struggling to complete successfully its IMF program. Thailand and Malaysia, however, have taken some action to quicken the pace of financial sector reform. On December 7, Thai authorities announced the closure of 56 of the 58 suspended finance companies; this action paved the way for the IMF's release of the second tranche of funds (about $0.8 billion) under the standby arrangement. On December 5, Malaysia's government unveiled a stabilization package that includes a sharp cut in government spending and measures to improve financial sector disclosure standards and performance. Market reaction to the measures has been positive as the stock price index rose almost 5 percent from the day of the announcement to December 10.

In **Hong Kong**, speculative pressures on the Hong Kong dollar had eased by early December, but were renewed upon concerns about Korea. The yield spread between Hong Kong government debt and U.S. Treasuries narrowed from 1150 basis points in late October to 350 basis points on December 10 at a one-year maturity, but the following day widened to 500 basis points. Despite the speculative pressure on the currency in late October and press reports of heavy intervention in foreign exchange markets by the Hong Kong Monetary Authority, foreign exchange reserves actually rose in October from the previous month. Reserves stood at $92 billion, up $4 billion from September. GDP grew 6.4 percent in the second quarter of 1997 (the latest period available) from a year earlier.

In **China**, output growth has continued to moderate in 1997, while inflation has remained low. In the first ten months of 1997, surging exports led to a trade surplus of nearly $36 billion, compared with a surplus of $8 billion in the year-earlier period. The value of exports rose 24 percent while the value of imports rose 4 percent from the year-earlier period. Import growth has been somewhat stronger since mid-year, with imports up 10 percent since June from the year-earlier period.

So far, China has remained relatively unaffected by the current financial crisis in Asia. China's exchange rate has remained stable against the U.S. dollar, while foreign exchange reserves have risen steadily; through September, foreign exchange reserves were up $29 billion for the year, reaching a level of $136 billion. China's currency is not convertible on the capital account, making a speculative attack difficult.

CHINESE ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1996	1997			1997		
		Q1	Q2	Q3	Aug	Sep	Oct
Real GDP[1]	9.7	9.4	9.5	9.0	...	...	...
Industrial Production	15.6	13.0	14.2	12.1	13.0	13.2	n.a.
Consumer Prices[2]	7.0	4.0	2.8	1.8	1.9	1.8	1.5
Trade Balance[3]	12.2	6.8	11.0	12.8	5.0	5.1	5.0

1. Cumulative from the beginning of the year
2. End of period
3. Billions of U.S. dollars, NSA

In **Taiwan**, output has grown strongly in recent months, while consumer prices have remained relatively flat. Strong import growth contributed to a narrowing of Taiwan's trade surplus in the first eleven months of 1997 to $7.8 billion, compared with a surplus of more than $11 billion in the comparable period last year. Exports rose 6 percent over this period, while imports rose 12 percent.

TAIWAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted, NSA)

	1996	1997			1997		
		Q1	Q2	Q3	Sep	Oct	Nov
Real GDP	5.7	6.8	6.3	6.9	...	...	...
Industrial Production	1.6	5.4	6.2	7.4	8.3	10.8	na
Consumer Prices[1]	2.5	1.1	1.8	0.6	0.6	-0.3	-0.5
Trade Balance[2]	14.3	1.8	1.7	2.0	1.1	1.0	1.3
Current Account[2]	10.5	1.9	1.0	2.1	...	...	...

1. End of period
2. Billions of U.S. dollars, NSA

As of December 10, the Taiwan dollar had depreciated 12 percent against the U.S. dollar since Taiwan's authorities announced on October 17 that they would no longer defend the currency. The stock market, which fell nearly 30 percent from mid-August to late October, had recovered nearly 20 percent as of December 11. At the end of October, international reserves were $83 billion, down $3 billion from a month earlier, and down $7 billion from their recent peak in June.

In **Brazil**, growth moderated in the third quarter, as real GDP was up by 4.1 percent (s.a.a.r.), compared with a whopping 14 percent growth in the second quarter. Indications are that economic activity has slowed since late October, when the central bank raised its discount rate from 21 to 43 percent. (The rate was subsequently lowered to 41 percent.) Inflation has continued to be remarkably low under the Cardoso government's 3-1/2 year-old stabilization program, the "Plano Real."

Downward pressures on the currency, the "real," have generally eased in recent weeks. However, at the end of the intermeeting period, financial conditions had begun to weaken again, apparently as a result of the turmoil in Korea. Interest rates on 30-day bank CDs, which skyrocketed from 20 percent in early November to 47 percent in mid-November, stood at 35 percent on December 10. The Bovespa stock price index, which had plunged by 35 percent between late October and mid-November, had regained over half of its earlier loss. Central Bank President Gustavo Franco and Finance Minister Pedro Malan have stated several times in recent weeks that the government has no intention of devaluing the "real."

BRAZILIAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1996	1997			1997		
		Q1	Q2	Q3	Sep	Oct	Nov
Real GDP, s.a.a.r.[1]	2.9	-2.2	13.9	4.1	...	...	...
Industrial Production (SA)[2]	2.3	-1.6	1.3	1.4	0.9	0.4	n.a.
Open Unemployment Rate (%)	5.4	5.6	5.8	5.8	5.6	5.7	n.a.
Consumer Prices[3]	9.4	2.0	1.0	0.4	0.1	0.3	0.2
Trade Balance[4]	-5.5	-3.1	-1.7	-2.2	-1.1	-0.8	-1.3
Current Account[4]	-24.3	-6.4	-8.4	-7.9	-2.9	-3.9	n.a.

1. Percent-change from previous period.
2. Annual data are from national income accounts.
3. INPC, Percentage change from previous period. Annual data are Dec/Dec.
4. Billions of U.S. dollars, NSA

The improvement in financial conditions followed the Cardoso government's unveiling of a package of 50 fiscal measures aimed at reducing the fiscal deficit by $20 billion in 1998 (2-1/2 percent of GDP). Prospects for fiscal tightening were strengthened when the House of Deputies approved a constitutional amendment that would enable federal, state, and local governments to cut their payrolls.

The government hopes that fiscal austerity will also cut the current account deficit, which is expected to be about 4 percent of GDP in 1997 and has fueled downward pressures on the "real." The cumulative trade deficit for the year through November was $9 billion, up considerably from a deficit of about $2 billion over the same period last year. Imports grew 25 percent over the period, while exports grew 10 percent.

In **Argentina**, economic activity continues to display strength. Industrial production rose 13 percent in October from its year-ago level, and real GDP grew by 8.6 percent in the third quarter from a year ago. Despite this, inflation remains non-existent. The stronger output growth has led to a trade deficit of over $2 billion through September this year, compared with a surplus of $1.6 billion over the same period in 1996.

Since the eruption of the currency crisis in Asia in late October, Argentine financial markets have experienced considerable turmoil. In the first few days of the crisis, the Argentine Central Bank lost about $1 billion in foreign currency (roughly 5 percent of reserves excluding gold), but reserves recovered in a short time and stood at just over $19 billion at the end of November, roughly the same level as at end-September. Total bank deposits from October 19 to November 19 actually grew by 2.5 percent, but peso-denominated deposits fell 3 percent, indicating a modest shift toward dollar-denominated deposits. The blue-chip Merval index fell some 30 percent from October 23 to November 12, when it reached a low-point for the year. Although it subsequently recovered much of its earlier losses, stock prices were dragged significantly down again this week by declines in world market.

ARGENTINE ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1996	1997			1997		
		Q1	Q2	Q3	Sep	Oct	Nov
Real GDP	4.3	8.2	8.2	8.6	...	...	...
Industrial Production (SA)	3.4	8.0	8.0	9.3	15.1	13.0	n.a.
Unemployment Rate (%)[2]	17.2	...	16.1	...	...	...	...
Consumer Prices[1]	0.1	0.4	-0.2	0.4	0.0	-0.2	-0.2
Trade Balance[3]	1.6	-0.4	0.0	-1.6	-0.6	n.a.	n.a.
Current Account[3]	-4.0	-2.4	-1.5	n.a.	...	...	...

1. Percentage change from previous period.
2. Unemployment figures available only in May and October of each year. The annual figure is the average of the two surveys.
3. Billions of U.S. dollars.

A major impact on Argentina of developments in Asia since late October has been high interest rates. The call money rate rose from 6.5 percent in late October to a peak of 13 percent in early November and since then has fallen to about 9 percent. Over this period, the peso-dollar deposit spread on 30-day deposits rose from about 50 basis points to a peak of 700 basis points, and has since fallen to 300 basis points. Argentine Brady bond spreads have displayed a similar pattern of movement.

After several months of discussions, the Argentine government has reached agreement on an IMF $2.8 billion Extended Fund Facility. The program will follow the current stand-by, which will expire at the end of this year. All performance criteria have been met.

Mexico's economy showed unexpected strength in the third quarter as real GDP rose 8.1 percent above its year-earlier level, or about 2 percent on a seasonally adjusted basis from the second quarter (not annual rate). The robust economy was mirrored in an even stronger showing for industrial production, and continued the rapid expansion registered earlier in the year. Recently, growth has become more broadly based. While manufactures, the focus of recovery after the 1995 recession, have continued to expand, output in the construction and service sectors also have grown strongly in the third quarter. Largely reflecting the rebound in domestic demand, the trade balance continued to deteriorate in recent months, leading to a correspondent widening of the current account deficit. However, inflation has remained subdued, with upticks in September and November largely reflecting seasonal factors.

MEXICAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1996	1997			1997		
		Q1	Q2	Q3	Sep	Oct	Nov
Real GDP	5.1	5.1	8.8	8.1	...	...	...
Industrial Production	10.4	6.3	11.3	10.4	13.0	n.a.	n.a.
Unemployment Rate (%)	5.5	4.3	3.9	3.7	3.4	3.2	n.a.
Consumer Prices[1]	27.7	5.6	2.9	3.0	1.2	0.8	1.1
Trade Balance[2]	6.3	1.5	0.6	-0.3	-0.2	-0.2	n.a.
Imports[2]	89.6	23.5	26.8	28.4	10.0	10.5	n.a.
Exports[2]	95.9	25.0	27.4	28.2	9.8	10.2	n.a.
Current Account[2]	-1.9	-0.3	-1.4	-2.5	...	...	...

1. Percentage change from previous period.
2. Billions of U.S. dollars, NSA

Mexican financial markets appear to have stabilized following the turmoil that was triggered by the sharp decline of the Hong Kong stock market at the end of October and its spillover into markets in other regions. The peso value of the dollar, after rising to over 8.4 at the end of October, has since returned to about 8.1 in recent trading, only 5 percent more depreciated than its mid-October level. At the most recent Treasury auction, 28-day interest rates registered 19.3 percent, still about 200 basis points above their mid-October level, but below their recent peak of 21.2 percent on November 11. Additionally, spreads on Mexican Brady bonds, adjusted for collateral, have declined to about 440 basis points from their recent peak of 600 basis points on November 12.

In **Venezuela**, the recent pick-up in economic activity continues. The economy grew by 4 percent in the first half of this year, and recent data on automobile sales and electricity usage indicate that this growth is continuing. The upward trend in recent months in inflation was reversed slightly in November. The growth in economic activity has led to an increase in imports, and the non-oil trade deficit has widened to $5 billion through September this year, compared with $3.6 billion over the same period in 1996. International reserves (excluding gold) stood at $15 billion at the end of November, about 25 percent higher than a year ago and roughly the same as at end-September. As a fallout of the Asian situation, the Caracas stock index has displayed considerable volatility and on net has fallen 20 percent since late October.

VENEZUELAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1996	1997			1997		
		Q1	Q2	Q3	Sep	Oct	Nov
Real GDP	-1.6	...	...	...	...	...	...
Unemployment Rate (NSA, %)	11.8	12.6	12.1	11.0	...	...	...
Consumer Prices[1]	103.3	6.6	7.5	9.8	3.4	3.8	2.8
Non-oil Trade Balance[2]	-4.8	-1.2	-1.6	-2.2	-0.8	n.a.	n.a.
Trade Balance[2]	13.8	3.3	2.8	2.4	0.8	n.a.	n.a.
Current Account[2]	8.8	...	...	...	...	...	...

1. Percentage change from previous period, NSA.
2. Billions of U.S. dollars, NSA.

In **Russia**, the most recent available macroeconomic indicators continue little changed. In October, output remained slightly above its year-earlier level and inflation continued to decline, dropping below 13 percent on a 12-month basis.

Financial markets have come under substantial pressure over the past month, reflecting spillover from financial market turmoil in Asia as well as concerns over the course of macroeconomic policy in Russia. The ruble has come under heavy selling pressure,

. According to Central Bank Chairman Dubinin, total reserves (gold and foreign exchange) declined nearly $5 billion in November to $18 billion. The existence of restrictions which prevent some foreign holders of ruble assets from immediately converting them into foreign currency--imposing a delay of a month--suggest that the November selling pressure may be reflected in further reserve losses in December. On November 10, the central bank moved to support the ruble by raising its main lending rate by 7 percentage points to 28 percent. On December 3, the central bank indicated that this rate would be adjusted up further, in line with the rise in market rates. Equity prices, which had risen very sharply earlier in the year, have fallen by over one-third on average from their peak levels of October.

RUSSIAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1996	1997			1997		
		Q1	Q2	Q3	Aug	Sep	Oct
Real GDP	-6.3	0	-0.8	1.1	1.1	2.3	0.5
Industrial Production	-5.2	0.9	0.9	2.2	3.0	0.3	2.3
Consumer Prices[1]	1.7	1.7	1.0	0.2	-0.1	-0.3	0.2
Ruble Depreciation[1]	1.5	1.0	0.7	0.6	0.6	0.4	0.4
Trade Balance[2]	23.1	5.9	n.a.	n.a.	...	...	...
Current Account[2]	9.6	3.4	n.a.	n.a.	...	...	...

1. Monthly rate.
2. Billions of U.S. dollars.

Recent political developments have raised questions over the future course of economic policy. A scandal over a book contract has led to the dismissal of several key economic reformers from their government positions, including the loss by First Deputy Prime Minister Chubais of his position as finance minister. President Yeltsin has suggested that there may be further personnel changes if his promise to pay all government wage arrears by the end of the year is not met. (This goal appears very unlikely, given the large size of these arrears--about $2 billion--and the continued substantial shortfall of tax receipts.) This apparent disarray in the government's policymaking apparatus has emboldened the opposition-controlled parliament to delay consideration of the government's proposed 1998 budget and key economic reform measures, including tax reform.